BanqueNationale
DE BELGIQUE
Eurosystème

Governance manual for stockbroking firms

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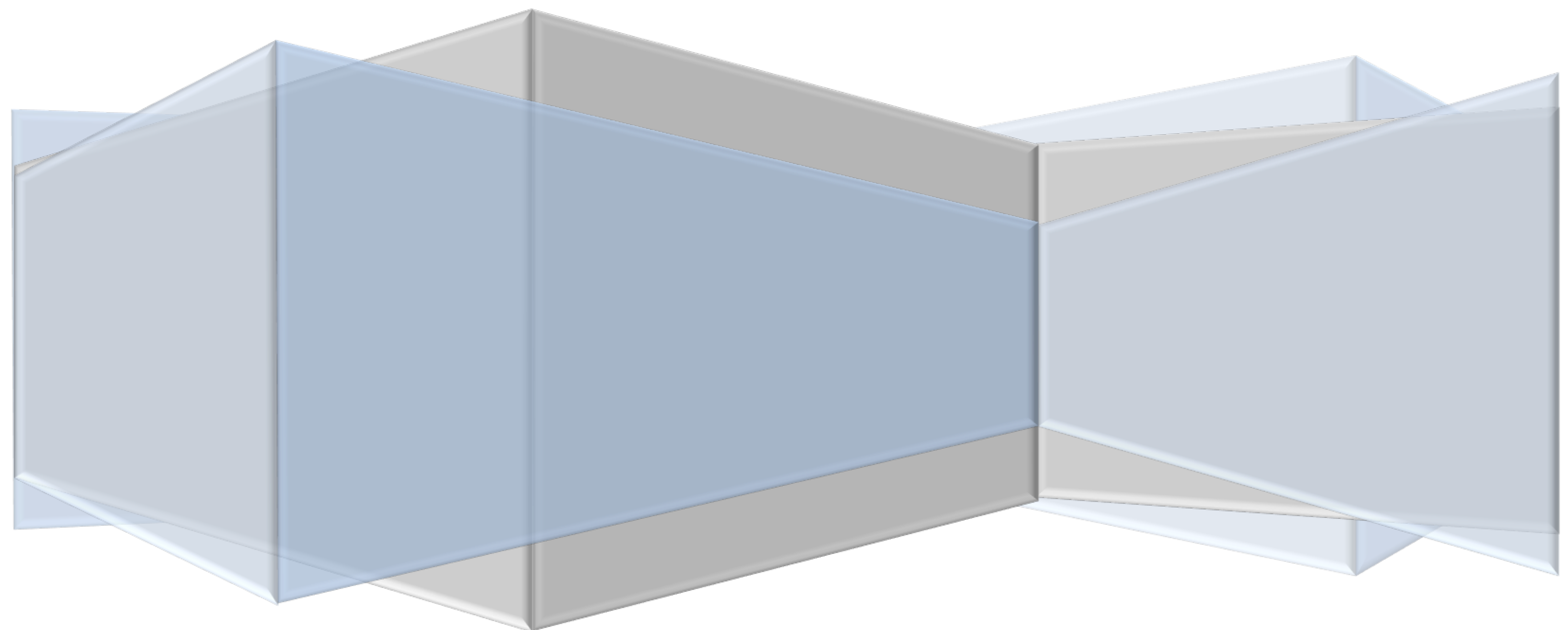

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0. OVERVIEW OF CHANGES

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1.INTRODUCTION

1:1 Corporate governance is key to the proper functioning of financial institutions and the financial and economic system.

1.1. CONTEXT

1:2 Stockbroking firms are, by definition, risky entities (giving rise to risks for customers, for themselves and for the market in general). Consequently, they are required to take measures to ensure a high degree of confidence in their stability and solvency/liquidity. A commitment to taking all reasonable measures to ensure the proper governance of their activities is thus important not only for the sake of their own management but also to maintain confidence on the part of the public, their customers and market participants in individual institutions and the financial system as a whole.

1:3 On 20 July 2022, as part of the transposition of the Investment Firms Directive (IFD),[1] Belgium adopted the Act on the legal status and supervision of stockbroking firms (the "Brokerage Supervision Act"),[2] laying down rules on sound governance. This act builds on previous legislation, including the Act of 25 October 2016 which incorporated rules on stockbroking firms into the Banking Act.

1:4 This manual has two objectives: on the one hand, to consolidate in a single document the legislative and regulatory provisions on sound governance that underpin the prudential supervision of stockbroking firms (without replacing the underlying documents) and, on the other hand, to clarify the NBB's prudential expectations in terms of governance by highlighting new elements resulting from the latest legislative and regulatory developments in this area.

1:5 To ensure compliance with the governance rules, the Brokerage Supervision Act places at the disposal of the National Bank of Belgium a broad range of measures: prudential measures in the framework of Pillar 2 (Article 138), recovery measures (Articles 202-207), penalties (Articles 235-237) and administrative fines (Article 238). In addition, certain violations may be criminally sanctioned (Articles 239-243).

1.2. SCOPE

1:6 This manual applies to the following institutions:[3]

- stockbroking firms established in Belgium, with the exception of large stockbroking firms[4] in classes 1A and 1B, which are subject, through references in the Brokerage Supervision Act, to the provisions of the Banking Act and the Governance Manual for the Banking Sector;[5] and
- Belgian branches of stockbroking firms governed by the law of a non-EEA Member;[6] and

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[1] Directive (EU) 2019/2034 of the European Parliament and of the Council of 27 November 2019 on the prudential supervision of investment firms and amending Directives 2002/87/EC, 2009/65/EC, 2011/61/EU, 2013/36/EU, 2014/59/EU and 2014/65/EU.

[2] Act of 20 July 2022 on the legal status and supervision of stockbroking firms.

[3] The applicable governance rules at group level, when a stockbroking firm forms part of a group of credit institutions that includes a credit institution governed by Belgian law or a financial conglomerate, are set out in Chapter 5 ("Governance at group level") of the Governance Manual for the Banking Sector. Please refer to that chapter for group aspects.

[4] These are stockbroking firms that:
- meet the conditions set out in Article 1(2)(a) or (b) of Regulation (EU) 2019/2033;
- are subject to a decision by the Bank pursuant to Article 91 of the Banking Act or Article 1(5) of Regulation (EU) 2019/2033; or
- form the object of a decision taken by the competent authority of the Member State where the stockbroking firm is authorised pursuant to the legislation of this Member State aimed at transposing Article 5 of Directive (EU) 2019/2034 or pursuant to Article 1(5) of Regulation (EU) 2019/2033.

[5] In other words, this manual concerns stockbroking firms falling within class 2, including small stockbroking firms that are subject to less stringent rules.

[6] Taking into account Article 226 of the Brokerage Supervision Act.

- investment holding companies and mixed financial holding companies governed by Belgian law that form part of a group of investment firms.[7]

1.3 METHODOLOGY

1:7 This manual aims to refer to all texts containing governance requirements (the Brokerage Supervision Act and its explanatory memorandum, regulations, royal decrees, circulars, communications, European legislation and EBA guidelines) and, where appropriate, to provide further clarification on these documents. It is thus intended to clarify the NBB's prudential expectations in terms of governance for a range of subjects. In addition, the manual addresses topics that are not per se covered by specific policy papers. It goes without saying that policy papers that are not touched on in this manual continue to apply. Furthermore, this manual is without prejudice to the governance powers of other supervisory authorities (e.g. the FSMA).

1:8 This manual does not replace the relevant policy papers. If such policy papers are amended, the manual will be adapted and should be interpreted in a dynamic manner in the meantime. As this manual is in principle an online publication, it is intended to be a constantly evolving (or "living") document that remains applicable as modifications are made, without changing its headings or references, as is the case for example with circulars that are not published in online format. Firms will, however, always be notified of any amendments made. In addition, these are explained in a specific section of the manual, with an indication of the date of amendment.

1:9 Insofar as possible, the structure of this manual follows that of the Brokerage Supervision Act and the EBA Guidelines of 22 November 2021 on internal governance for investment firms (EBA/GL/2021/14).

1:10 This manual also transposes into Belgian law the EBA Guidelines on internal governance for investment firms (EBA/GL/2021/14) and the EBA Guidelines on remuneration policies for investment firms (EBA/GL/2021/13) under the Investment Firms Directive, which are appended hereto.

1:11 This manual covers the following topics: (i) qualities required of shareholders or partners, (ii) suitability of management and the independent control functions, (iii) appropriate organisation of the business, (iv) governance at group level, and (v) prudential reporting and transparency.

1.4. PROPORTIONALITY

1:12 Article 17 §4 of the Brokerage Supervision Act provides that internal governance arrangements must be proportionate to the nature, scale and complexity of the risks inherent in the firm's business model and operations.

1:13 Pursuant to the principle of proportionality, stockbroking firms falling within the scope of this manual may take into account criteria such as the nature, scale and complexity of the risks inherent in their business model and operations in order to determine the level of governance requirements applicable to them.

1:14 In practice, the NBB relies on the concept of a "small stockbroking firm" to apply the principle of proportionality. The implications of this can be seen, for instance, in the following areas: management structure (senior management, specialised committees, independent directors and positioning of the CRO), internal control and the independent control functions (less sophisticated internal policies and the possibility to combine the risk management and compliance functions), frequency of reporting (assessment report on

[7] The applicable rules of governance at group level when a stockbroking firm belongs to a group of investment firms are set out in Chapter 5 ("Governance at group level") of this manual. When a stockbroking firm belongs to a group that includes a credit institution, the rules on the supervision of groups set out in the Banking Act apply and reference is thus made to the Governance Manual for the Banking Sector with regard to these aspects.

the internal control system to be submitted every two years), etc. For more information on the principle of proportionality and the criteria to be taken into account, please see paragraphs 17 to 21 of EBA/GL/2021/14.

1.5 DEFINITIONS

1:15 The terms used in this manual have the same meaning as in Article 3 of the Brokerage Supervision Act or in EBA/GL/2021/14. For purposes of this manual, the following definitions apply.

1:16 "**Brokerage Supervision Act**": the Act of 20 July 2022 on the legal status and supervision of stockbroking firms.

1:17 "**CAC**": the Companies and Associations Code, introduced by the Act of 23 March 2019.

1:18 **"Directors"**: all members of the statutory governing body of a stockbroking firm, an investment holding company or a mixed financial holding company falling within the scope of this manual, including both executive and non-executive directors.

1:19 **"Diversity"**: the situation whereby the characteristics of the members of the statutory governing body, including their age, gender, geographical provenance[8] and educational and professional background, are different to an extent that allows for a variety of views within this body.

1:20 "**Independent control functions**": the risk management function, the compliance function and the internal audit function.[9]

1:21 "**NBB**": the National Bank of Belgium.

1:22 "**Senior managers**": the persons making up the firm's senior management,[10] namely:
a) where a management committee has been set up, the members of this committee and any other person whose position is at the next lower hierarchical level, insofar as that person can have a direct and decisive influence on the management of all or some of the firm's activities, including the managers of foreign branches;
b) where such a committee has not been established, any persons who can have a direct and decisive influence on the management of all or some of the firm's activities.

1:23 "**Small stockbroking firm**":[11] a stockbroking firm whose asset value (on-balance sheet and off-balance sheet) was, on average, less than or equal to €300 million over the four-year period immediately preceding the current financial year.

1:24 Furthermore, the term "**firm**" in this manual should be interpreted as referring to stockbroking firms falling within the scope of application set out above.

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8 The term "geographical provenance" refers to the region where a person has gained a cultural, educational or professional background. This aspect is particularly important for firms that are active internationally.

9 In Belgium, these three mandatory independent control functions constitute the "key functions" referred to in EBA/GL/2021/14.

10 See the definition of "senior management" in the NBB Regulation of 9 November 2021 on the exercise of external functions. This concept is similarly defined in Article 3(63) of the Brokerage Supervision Act.

11 See Article 23 of the Brokerage Supervision Act. It should be noted that Belgium chose to exercise the option offered to the Member States to raise the threshold from €100 million to €300 million, thereby extending the special regime applicable to "small stockbroking firms" to a larger number of firms, in accordance with Article 32(4)(a) and (5) of Directive (EU) 2019/2034.

2. QUALITIES REQUIRED OF SIGNIFICANT SHAREHOLDERS

Statutory and regulatory framework

1. Brokerage Supervision Act: Articles 6, 14, 45 to 54, 83 and 227

2. NBB circulars:
- Communication NBB_2017_22 of 14 September 2017 to potential shareholders and transferring shareholders
- Circular NBB_2017_23 of 14 September 2017 to financial institutions on acquisitions, increases, reductions and disposals of qualifying holdings

3. International reference documents:
- Joint Guidelines of the EBA, EIOPA and ESMA of 5 May 2017 on the prudential assessment of acquisitions and increases of qualifying holdings in the financial sector

2.1 PRUDENTIAL EXPECTATIONS

2:1 From a prudential point of view, it is essential that significant shareholder(s) have the qualities necessary to ensure that they exercise their influence to promote sound and prudent management and development of the business on a going concern basis. They should also take into account the prudential expectations in terms of governance that are incumbent on investment firms.

2:2 This prudential requirement is a prerequisite for obtaining a licence and continues to apply to the firm during the exercise of its activities. It is reflected in particular in the mandatory prudential assessment of the qualities of natural or legal persons that decide to acquire or significantly increase a qualifying holding in the firm's capital.

2:3 Shareholders with a qualifying holding ("qualifying shareholders"), as well as the firm itself upon learning of such a holding, should notify the NBB of any change (an increase or reduction that causes certain thresholds to be crossed) in the firm's capital structure.

2:4 The firm should provide the NBB with all relevant information on its qualifying shareholders of which it is aware and which could have an influence on the prudential assessment of these shareholders. This obligation also applies to the shareholders concerned.

2.2 SUITABILITY ASSESSMENT

2:5 The prudential assessment criteria, both in the context of the licence application process and afterwards, are explained in the Joint Guidelines of the EBA, EIOPA and ESMA on the prudential assessment of acquisitions and increases of qualifying holdings in the financial sector. Existing and potential shareholders should read this document in conjunction with Communication NBB_2017_22. The rules applicable to stockbroking firms are specified in Circular NBB_2017_23.

2.3. FAMILY/PARTNERS' CHARTER

2:6 Family-owned stockbroking firms or those whose shareholder structure consists of a limited number of partners are recommended to draw up a charter governing relations between the family members or partners, on the one hand, and the stockbroking firm, on the other hand, as regards sound governance, corporate vision, financial objectives, the oversight of management, career paths, remuneration, etc.

2.4. PROHIBITION ON GRANTING LOANS, CREDIT OR GUARANTEES TO ACQUIRE SHARES

2:7 No loans, credit or guarantees may be granted, directly or indirectly, to persons to enable them to directly or indirectly acquire or subscribe to shares or other securities that confer a right to dividends of the firm or a closely connected company or that confer the right to acquire such securities. This type of transaction, whereby the repayment or cancellation of the resulting obligation depends to a certain extent on the distribution of dividends by the firm, undermines the loss-absorbing capacity of the capital thus financed.

3. SUITABILITY OF DIRECTORS, SENIOR MANAGERS AND HEADS OF INDEPENDENT CONTROL FUNCTIONS

Statutory and regulatory framework

1. Brokerage Supervision Act: Articles 3(64), 15, 16, 61 to 64, 83 and 98
2. NBB regulations:
   - Royal Decree of 8 February 2022 approving the NBB Regulation of 9 November 2021 on the exercise of external functions by managers and heads of independent control functions of regulated undertakings
3. NBB circulars:
   - Communication NBB_2022_34 of 22 December 2022 updating the Fit & Proper Manual
   - Communication NBB_2022_19 of 12 July 2022 on the exercise of external functions by managers and heads of independent control functions of regulated undertakings
   - Circular NBB_2021_27 of 16 November 2021 transposing EBA/GL/2021/06 on the assessment of the suitability of members of the management body and key function holders
   - Circular NBB_2018_25 of 18 September 2018 on the suitability of directors, members of the management committee, persons responsible for independent control functions and senior managers of financial institutions (introducing the NBB's Fit & Proper Manual)
   - Circular NBB_2017_21 of 7 July 2017 on the extension of loans, credit and guarantees to managers, shareholders and related persons
4. International reference documents:
   - EBA/GL/2021/14 – Guidelines on internal governance for investment firms under Directive (EU) 2019/2034
   - EBA/GL/2021/06 – Guidelines on the assessment of the suitability of members of the management body and key function holders

3.1. FIT & PROPER

3.1.1. GENERAL INFORMATION

3:1 Pursuant to Article 15 of the Brokerage Supervision Act, the directors, senior managers and heads of the independent control functions of stockbroking firms must at all times meet the fitness and propriety criteria required for their role. The suitability assessment of these persons forms part of what is often referred to as the "fit & proper" assessment.

3:2 The fit & proper assessment is primarily the responsibility of the firm itself, but the NBB is also empowered to assess whether candidates possess the required qualities. Pursuant to Articles 61 and 62, nominations must be notified and submitted for prior approval to the NBB.

3:3 The NBB's Fit & Proper Manual (Chapter 3) clarifies the criteria to be used for the fit & proper assessment, specifies what is expected of the firms in this regard, and sets out the fit & proper policy implemented by the NBB in terms of both content and procedure.

3.1.2. SENIOR MANAGEMENT

3:4 In the statutory "fit & proper" provisions, the concept of "senior management" is an important one. This term is defined in Article 1(11) of the NBB Regulation of 9 November 2021 on the exercise of external functions by managers and heads of independent control functions of regulated undertakings and in Article 3(63) of the Brokerage Supervision Act.

3:5 According to this definition, a senior manager is a person that participates in the stockbroking firm's effective management, namely:

a) when a management committee has been established, the members of this committee and any other person whose position is at the next hierarchical level down, insofar as they can exercise direct and decisive influence on the management of all or some of the firm's activities, including the managers of foreign branches;
b) when such a committee has not been established, any persons who can exercise direct and decisive influence on the management of all or some of the firm's activities.

3:6 Senior management thus consists of the members of the management committee and the persons at a hierarchical level immediately below this committee (the so-called "MC-1" level), insofar as these persons can exercise direct and decisive influence on the management of all or some of the firm's activities.

3:7 Where the firm has not set up a management committee,[12] "senior management" is understood to mean the executive directors and those persons who, without having the capacity of director, qualify as senior managers due to their ability to exercise direct and decisive influence over the management of all or some of the firm's activities.

3:8 Furthermore, pursuant to Article 98 of the Brokerage Supervision Act, the managers of foreign branches (in the EEA or a third country) are also considered members of senior management.

3:9 The firm itself decides who forms part of its senior management. For several years now, the NBB has recommended that the statutory governing body draw up a list, by way of a formal decision, of the names and/or functions of those persons who, without being directors, qualify as senior managers.

3:10 Although all senior managers should individually possess the qualities listed in Article 15 of the Brokerage Supervision Act, the appointment - in firms with a management committee - of senior managers who are not members of either the management committee or the statutory governing body need not be notified in advance or submitted for approval to the NBB. This concerns in particular persons at a hierarchical level immediately below that of the management committee who have a direct and decisive influence on the management of all or some of the firm's activities (MC-1 level). These persons should have the qualities required of senior managers pursuant to Article 15 of the Brokerage Supervision Act. The firm is primarily responsible for ensuring that this is the case. However, as explained in the Fit & Proper Manual, compliance with the above conditions in respect of these persons is not subject to prior approval by the NBB on the basis of Article 61 of the Brokerage Supervision Act but rather is monitored as part of its ongoing supervision of the firm.

3.1.3. STAFF MEMBERS OF THE FIRM

3:11 Although the fit & proper assessment provided for by the Brokerage Supervision Act has a limited *ratione personae* scope, it is recommended that the prudential expectations regarding the fit & proper assessment specified in the NBB's Fit & Proper Manual be taken into account in the recruitment, assessment and training of all staff of a stockbroking firm. This subject forms part of ongoing governance monitoring (see the sections on "Organisational set-up" and "Internal control framework" in this manual).

3.2. EXTERNAL FUNCTIONS

3:12 Pursuant to Articles 62 and 63 §1 of the Brokerage Supervision Act, members of the statutory governing body, senior managers and heads of the independent control functions must devote sufficient time to the exercise of their functions within the firm. This general principle of availability is laid out in Article 63 §§1 to 9 of the Brokerage Supervision Act and in the NBB Regulation of 9 November 2021 on the exercise of external functions by the managers and heads of independent control functions of regulated undertakings.

[12] Unlike the Banking Act, the Brokerage Supervision Act does not require that a management committee be set up. The firm may establish a management committee on a voluntary basis or the NBB may require a management committee to be set up where the firm's size, internal organisation or activities so justify.

3:13 In brief, firms should adopt and comply with internal rules on external functions that pursue three objectives, namely to (i) ensure availability, (ii) prevent conflicts of interest, and (iii) ensure the disclosure of external functions. Firms should carry out a concrete assessment of the impact of the performance of external functions on managers and the heads of independent control functions. In this context, prior approval must be granted by the statutory governing body or senior management on the basis of a file the minimum content of which is laid down in the NBB Regulation of 9 November 2021. Firms are obliged to disclose external functions (except those exercised by the heads of independent control functions) in their annual report or on their website and to notify the NBB of the same using the fit & proper forms.[13]

3:14 For more information on the exercise of external functions, please see the NBB Regulation of 9 November 2021 and Communication NBB_2022_19 of 12 July 2022.

3.3. LOANS TO MANAGERS

3:15 Article 83 of the Brokerage Supervision Act contains provisions on loans, credit and guarantees provided by stockbroking firms[14] to their managers, shareholders and related persons. These provisions are further clarified in Circular NBB_2017_21 on loans, credit and guarantees to managers, shareholders and related persons.

3:16 Article 83 of the Brokerage Supervision Act provides for an obligation for firms to notify the NBB of loans, credit, guarantees and other transactions exceeding €100,000.

3:17 For more information, please see Circular NBB_2017_21 on loans, credit and guarantees to managers, shareholders and related persons and paragraphs 110 to 119 of EBA/GL/2021/14.

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[13] More specifically, Article 63 §8 of the Brokerage Supervision Act provides that the NBB must be notified without delay of external functions performed by directors and senior managers, with the exception of senior managers at N-1 level (excluding the heads of independent control functions). In practice, this limitation on the scope of application concerns only the notification of new external functions performed during the exercise of another function (using the "New information - New external function" form). This limitation is also without prejudice to the obligation for firms to update annually the eManex platform, which is intended to provide an overview of all external functions performed by directors, senior managers and the heads of independent control functions.

[14] Article 83 of the Brokerage Supervision Act does not apply to investment holding companies or mixed financial holding companies.

4. APPROPRIATE ORGANISATION OF THE BUSINESS

4:1 The requirement of sound and appropriate structures for organisation of the business to ensure effective and prudent management of the firm is described in Article 17 of the Brokerage Supervision Act. This is an essential statutory requirement inherent in the legal status of stockbroking firms. It must be complied with in all cases; only the scope and magnitude of this obligation vary depending on the nature, scale and complexity of the risks inherent in the firm's business model and operations (application of the principle of proportionality). The management structure should be continually adapted to the development of the firm's business. This requirement is reflected in the Brokerage Supervision Act by means of a non-exhaustive list of various aspects, which are covered in more detail below.

4.1. MANAGEMENT STRUCTURE

4.1.1. GENERAL REQUIREMENTS

Statutory and regulatory framework

1. Brokerage Supervision Act: Articles 17 §1(1), 29 and 56
2. NBB circulars: /
3. International reference documents:
   - EBA/GL/2021/14 => paragraphs 22 to 60

4:2 The firm must have a transparent management structure which ensures effective and prudent management in the light of the nature, scale and complexity of the risks inherent in its business model and operations.

4:3 Pursuant to Article 17 of the Brokerage Supervision Act, as a basic rule, there must be a division at the highest level between the functions responsible for effective management and those responsible for the supervision thereof. The following functions must be in place:

- a general policy function, responsible for determining general policy and strategy;
- a management function, responsible for managing the firm's activity; and
- a supervisory function, responsible for supervising management.

4:4 The Brokerage Supervision Act provides for a *sui generis* governance model.[15] In stockbroking firms, the general policy function is entrusted to the executive and non-executive directors on the statutory governing body, the management function is entrusted to the senior managers,[16] and the supervisory function is entrusted to the non-executive directors, in particular (but not exclusively) the members of specialised committees of the statutory governing body established pursuant to the Brokerage Supervision Act (the risk committee and the remuneration committee) or on a voluntary basis.[17]

4:5 The firm should clearly define the responsibilities for management and the supervision of management. The management function should determine the competencies and responsibilities of each segment of the organisation, specify the procedures and reporting lines and monitor their application. The interaction between the management function and the supervisory function should be efficient and constructive.

4.1.2. STATUTORY GOVERNING BODY

[15] Notwithstanding specific provisions of the Brokerage Supervision Act due to the *sui generis* governance model, the general provisions of the CAC remain applicable.

[16] Senior managers may be executive directors as well as persons who, without having the capacity of director, are considered by the firm as *de facto* managers due to their ability to directly and decisively influence the management of all or some of the firm's activities.

[17] Article 24 (and Article 25 for small stockbroking firms) of the Brokerage Supervision Act.

Statutory and regulatory framework

1. Brokerage Supervision Act: Articles 19, 20, 29, 32 §2, 56 to 58, 61 §3 and 64
2. NBB circulars:
   - Circular NBB_2024_03 transposing EBA Guidelines 2023/08 of 18 December 2023 introducing new reporting obligations on diversity practices for credit institutions and stockbroking firms
   - Communication NBB_2023_04 on diversity - EBA and NBB benchmarking exercises and prudential expectations
   - Communication NBB_2022_34 of 22 December 2022 updating the NBB's Fit & Proper Manual
   - Circular NBB_2021_27 transposing EBA/GL/2021/06 on the assessment of suitability of members of the management body and key function holders
   - Communication NBB_2021_04 of 19 January 2021 on the HIVE project and the digitalisation of the fit & proper process
   - Communication NBB_2018_05 of 8 February 2018 on the report of the statutory governing body on assessment of the compliance function
3. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 22 to 32 and 36 to 43

4.1.2.1. Composition

4.1.2.1.1. Members and status

4:6 The statutory governing body is composed of both non-executive directors and executive directors (i.e. members of senior management or, where applicable, of the management committee). In order to safeguard the supervisory function of the statutory governing body, a majority of its members should be non-executive directors and it cannot be chaired by a person who is involved in senior management or, where applicable, a member of the management committee.[18] Day-to-day management, where provided for by the CAC for the relevant corporate form, cannot be assigned to a non-executive member of the statutory governing body.[19]

4:7 The size of the statutory governing body is determined based on the nature, scale and complexity of the firm's activities, its internal organisation and its capital structure. It should be sufficiently small to allow for effective decision-making, but large enough to ensure that directors bring experience and knowledge from fields relevant to the firm's proper management and that changes to its composition can be managed without undue disruption, in order to ensure continuity.

4:8 Pursuant to Article 15 of the Brokerage Supervision Act, the (executive and non-executive) members of the statutory governing body must be natural persons.

4:9 In terms of employment status, a directorship of a stockbroking firm may not be exercised within the framework of an employment contract (in other words, it must be performed in a self-employed capacity) and combining two statuses (i.e., self-employed and employee) within the same firm or a company in which the firm holds a stake is incompatible with the principles of sound governance applicable to stockbroking firms[20] (Article 64 of the Brokerage Supervision Act). However, exceptions are possible if the firm is required to comply with obligations of foreign law that require the presence of employees on the statutory governing body.

4.1.2.1.2. Independent directors within the meaning of Article 3(64) of the Brokerage Supervision Act

4:10 The independent non-executive directors should specifically ensure that the decision-making process takes into account the interests of all internal and external stakeholders, including minority shareholders, investors, etc. In this way, they contribute to the supervision of management.

[18] This does not apply to small stockbroking firms pursuant to Article 20 §2 of the Brokerage Supervision Act.
[19] This does not apply to small stockbroking firms pursuant to Article 20 §2 of the Brokerage Supervision Act.
[20] These principles include independence of mind, collective decision-making by the statutory governing body, etc.

4:11 Pursuant to Article 24 of the Brokerage Supervision Act, firms that are required to establish a risk committee and a remuneration committee must ensure that each of these committees includes at least one independent director. However, small stockbroking firms that are exempt from the obligation to establish a risk committee and a remuneration committee pursuant to Article 25 of the Brokerage Supervision Act are not required to have an independent director.

4:12 Prior to the entry into force of the CAC, the Brokerage Supervision Act referred to Article 526*ter* of the former Company Code with regard to the definition of an independent director and the criteria to be met in this regard. These requirements are now set out in Article 3(64) of the Brokerage Supervision Act and refer to the criteria in EBA/GL/2021/14. Failure to meet one of the independence criteria does not automatically mean that the person concerned can no longer be considered independent. The firm may demonstrate to the NBB that, although not all criteria have been met, the independence of the person concerned is not compromised (the "comply or explain" principle). In this case, the firm should submit a request for an exemption. The NBB will then decide whether to grant the request.[21]

4.1.2.1.3. Selection of directors – suitability and diversity

4:13 Directors should at all times be of sufficiently good repute and have adequate expertise, both individually and collectively, for the performance of their duties.

4:14 Specifically, directors should: (i) be of sufficiently good repute; (ii) possess sufficient knowledge, skills and experience to perform their duties; (iii) be able to act with honesty and independence of mind; (iv) be able to commit sufficient time to perform their functions; and (v) contribute to the collective suitability of the statutory governing body and, where appropriate, the management committee.

4:15 With regard to collective suitability, the statutory governing body should at all times possess adequate knowledge, skills and experience to be able to understand the firm's activities, including the main risks to which it is exposed.[22] In terms of the areas of competence to be represented on the statutory governing body, please refer to the NBB's Fit & Proper Manual (Chapter 3).

4:16 The composition of the statutory governing body should also be diverse in terms of gender, educational and professional background, age and - for firms that are active internationally - geographical provenance. Indeed, having a range of backgrounds, experience, values, opinions and views within the statutory governing body improves the process for taking decisions on strategy and risk-taking within the firm. The promotion of diversity is anchored in the Brokerage Supervision Act. For instance, Article 29 of the Brokerage Supervision Act obliges firms to use diversity as a criteria for the composition of the statutory governing body and to draw up a diversity policy that at least refers to the above aspects.

4:17 In the area of gender diversity in particular, the Brokerage Supervision Act considers gender balance of particular importance for ensuring an adequate representation of society on the governing bodies of stockbroking firms. In this regard, the legislation provides for the setting of a target for the representation of the under-represented gender on the statutory governing body and for the development of a plan to increase the number of representatives of this gender in order to reach the target. The target should be quantitative (a percentage of targeted participation by the under-represented gender) and defined for the statutory governing body collectively. If the management committee is large enough, the target may be split between the statutory governing body and this committee. This target, the aforementioned plan and the arrangements for its implementation must be made public in accordance with Article 48(b) of Regulation No 2019/2033 and notified to the NBB. When setting diversity objectives, firms should consider the results of the EBA's diversity benchmarking report.

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[21] The NBB generally takes a decision at the same time on the suitability of the person concerned and the request for exemption from a criterion set out in Article 3(64) of the Brokerage Supervision Act. However, these decisions may be taken separately if the issue of independence has a broader scope and implications for sound governance.

[22] The monitoring of collective suitability forms part of both sound governance and fit & proper supervision (collective suitability being an aspect of adequate expertise).

4:18 As part of their annual review of the composition of the statutory governing body, firms should document their compliance with the objectives and targets set. In the event diversity objectives or targets have not been met, firms should document the reasons for this, the measures to be taken and the timeframe for these measures, in order to ensure that the diversity objectives and targets are met. Certain stockbroking firms must also report to the NBB on diversity in accordance with circular NBB_2024_03.

4.1.2.1.4. Chair of the statutory governing body

4:19 The chair of the statutory governing body leads this body, contributes to the efficient flow of information within and between this body, its specialised committees and senior managers (and where applicable, the management committee) and is responsible for its effective overall functioning. For more information on the specific tasks of the chair, please see paragraphs 39 to 43 of EBA/GL/2021/14.

4.1.2.2. Tasks

4:20 Article 19 of the Brokerage Supervision Act provides that the statutory governing body assumes general responsibility for the firm. It does so in particular through exercise of the two functions described below.

4.1.2.2.1. General policy function

4:21 The main task of the statutory governing body is to establish the firm's strategy and general policy.

4:22 The statutory governing body is expected to determine the firm's strategy and targets, as well as its organisation for the provision of investment services, the conduct of investment activities and the provision of ancillary activities; the skills, knowledge and expertise required from staff; and the resources, procedures and mechanisms with or according to which the firm provides services and carries out its activities. This responsibility extends to capital adequacy, outsourcing, business continuity, customer acceptance, conflicts of interest, and protection of the rights of customers with regard to assets held by the firm.

4:23 The statutory governing body defines the firm's risk policy and determines its risk tolerance for all activities. It is expected to be primarily responsible for taking strategic decisions with regard to risks and is closely involved in the ongoing monitoring of the development of the firm's risk profile. Therefore, the statutory governing body should at all times possess relevant and comprehensive information on the risks to which the firm is exposed.

4:24 Furthermore, the statutory governing body defines the firm's fit and proper, integrity and remuneration policies. In accordance with Article 19 of the Brokerage Supervision Act, it also approves the governance memorandum.

4:25 For more information on the tasks of the statutory governing body, please see the Brokerage Supervision Act and paragraphs 22 to 31 of EBA/GL/2021/14.

4.1.2.2.2. Supervisory function

4:26 The supervision of the business and regular assessment of the firm's governance structure, organisation and internal controls constitute the second major area of responsibility entrusted to the statutory governing body.

4:27 Pursuant to Article 56 of the Brokerage Supervision Act, the statutory governing body must periodically, and at least once a year, assess the effectiveness of the firm's organisational structure, including specific organisational provisions related to the registration of investment services, the safeguarding of customer rights, the distinction between assets held for customers and its own assets, the validation process for financial instruments intended for sale, and the holding of funds. In addition, it must periodically monitor and evaluate the appropriateness and implementation of the firm's strategic objectives in relation to the provision of investment services, the conduct of investment activities and the provision of ancillary services.

4:28 The statutory governing body should also assess the proper functioning of the independent control functions. In addition to its regular contacts and the information provided to it by these functions, the statutory governing body should rely in particular on the periodic report of senior management or, where applicable, the management committee. It should also ensure that senior management takes the necessary measures to remedy any shortcomings. The statutory governing body shall provide the NBB with an annual report on assessment of the compliance function, in accordance with Article 32 §2 of the Brokerage Supervision Act.

4:29 Responsibility for overseeing the firm's operations lies with the statutory governing body in its supervisory capacity, in particular the non-executive directors who constitute the majority of this body. These directors should work in a coordinated manner to ensure the adequate exercise of supervision. Supervision may notably be based on the following:

- reporting by the independent control functions;
- effective use of the investigative powers vested in the members of the statutory governing body;
- reporting on the development of the firm's business by senior management to the statutory governing body; and
- exercise of the right to access the information and documents needed to carry out its tasks, which may include minutes of meetings of senior management or, where applicable, of the management committee.[23]

4:30 The exercise of such supervision presupposes that information and proposals formulated by members of senior management are critically evaluated and, if necessary, challenged, to ensure that decisions are taken with full knowledge of the facts.

4:31 For more information, please see paragraphs 36 to 38 of EBA/GL/2021/14.

4.1.2.3. Functioning

4:32 The statutory governing body takes decisions in a collective manner. In accordance with Article 29 of the Brokerage Supervision Act, the nomination committee should ensure that the decision-making of the statutory government body is not dominated by a single individual or a small group of individuals in such a way as to harm the interests of the firm as a whole.

4:33 The minutes of meetings of the statutory governing body shall summarise the discussions held, record the decisions taken and specify the questions and diverging views expressed by directors, in accordance with paragraph 3.8 of the Corporate Governance Code published by royal decree on 12 May 2019.

4:34 It is recommended that the statutory governing body adopt by-laws[24] describing its composition, tasks and functioning. The NBB recommends that these by-laws be annexed to the governance memorandum.

4:35 The statutory governing body must meet on a sufficiently regular basis to carry out its duties effectively. It is recommended that a strategy meeting be held at least once a year.

4:36 The statutory governing body should regularly assess the functioning of the management structure, including the powers, composition, size and number of meetings of the management bodies, as well as the individual attendance of directors. External experts may be called upon to carry out this assessment. Pursuant to Article 29 of the Brokerage Supervision Act, the nomination committee also has an important role to play in this regard. The NBB's Fit & Proper Manual and EBA/GL/2021/06 specify the situations in which the individual or collective suitability of members of the statutory governing body should be reassessed.

[23] See Article 56 §1, third subparagraph, of the Brokerage Supervision Act. The minutes of meetings of senior management or, where applicable, the management committee must be made available to all directors via a secure IT tool.

[24] The by-laws do not necessarily have to meet the conditions set out in Article 2:59 CAC.

4:37 The non-executive directors should assess their interaction with the executive directors at least once a year, where appropriate in the absence of the latter. The conclusions of these assessments, as well as the measures taken to improve the functioning of the management structure, should be set down in a report.

4:38 When a firm wishes to appoint a new director or to renew the term of office of an existing director, decides not to renew a director's term of office or to remove a director from office or is informed of a director's resignation, it must notify the NBB in advance in accordance with Article 61 §1 of the Brokerage Supervision Act. Pursuant to Article 61 §3 of this act, the firm should inform the NBB of any division of tasks between the members of its statutory governing body. Material changes to this division of tasks require the prior approval of the NBB.[25]

4:39 The members of the statutory governing body should undergo induction and training in accordance with paragraphs 95 to 101 of EBA/GL/2021/06. This training should enable them to have a clear understanding of the relevant laws, regulations and administrative provisions, the firm's structure, business model, risk profile[26] and governance arrangements, as well as their role. In accordance with Article 56 §3, second subparagraph, of the Brokerage Supervision Act, the statutory governing body shall ensure that the firm dedicates sufficient human and financial resources to the ongoing training of its personnel. Please refer to the NBB's Fit & Proper Manual for more information on this subject.

4.1.3. SENIOR MANAGEMENT (OR, WHERE APPLICABLE, THE MANAGEMENT COMMITTEE)

Statutory and regulatory framework

1. Brokerage Supervision Act: Articles 21, 22, 59, 60 and 61 §3
2. NBB circulars:
   - Communication NBB_2022_34 of 22 December 2022 updating the NBB's Fit & Proper Manual
   - Circular NBB_2021_27 transposing EBA/GL/2021/06 on the assessment of suitability of members of the management body and key function holders
   - Communication NBB_2021_04 of 20 January 2021 on the HIVE project and digitalisation of the fit and proper process
   - Circular NBB_2011_09 of 20 December 2011 on the assessment report by senior management on the internal control system, the assessment report by senior management on the internal controls as regards investment services and activities, and the statement by senior management on periodic prudential reporting
3. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 32 to 35

4:40 The management function is entrusted to senior management.

4:41 In accordance with Article 21 of the Brokerage Supervision Act, the NBB may require that a management committee be set up where the firm's size, internal organisation or activities so justify.[27] A management committee should enhance the efficiency of dual supervision and collective decision-making on the conduct of the firm's activity. The firm may also set up a management committee on a voluntary basis provided it informs the NBB of its intention to do so and the NBB does not object within 30 working days. The establishment of a management committee should be provided for in the firm's articles of association.

4.1.3.1. Composition

Members and status

[25] See footnote 129 to the NBB's Fit and Proper Manual.

[26] Including in relation to environmental and climate-related risks.

[27] The option for the NBB to require that a management committee be set up also applies to small stockbroking firms.

4:42 Senior management should consist of at least two persons holding a position that enables them to exercise effective reciprocal supervision (dual supervision). The NBB recommends that there preferably be three or more, to avoid deadlock.

4:43 Senior managers may be executive directors as well as persons who, without having the capacity of director, are considered by the firm as de facto managers due to the direct and decisive influence they can exercise over the management of all or some of its activities. The senior manager to whom daily management of the firm is delegated (for corporate forms where this possibility exists) must be an executive director.

4:44 Where a management committee has been set up, Article 21 §4 of the Brokerage Supervision Act requires that it be comprised exclusively of members of the statutory governing body.[28]

4:45 The NBB recommends that senior management or, where applicable, the management committee be comprised of at least the three following functions: the chief executive officer, the chief financial officer and the chief risk officer.

4:46 Members of senior management or, where applicable, the management committee must be natural persons who meet the (individual and collective) suitability requirements set out in the NBB's Fit & Proper Manual. Where they are members of the statutory governing body, they must perform their duties in a self-employed capacity (without exception).[29] If the composition of senior management or, where applicable, the management committee, is mixed (i.e. one or more executive directors and one or more non-directors), the non-director senior managers must also have self-employed status.[30]

Chief executive officer

4:47 The appointment of a chief executive officer or CEO (or, where applicable, a chair of the management committee) contributes to the efficient and coherent overall functioning of stockbroking firms and to the efficient flow of information with the statutory governing body.

Chief financial officer

4:48 The Brokerage Supervision Act does not require the chief financial officer (CFO) to be a member of senior management or, where applicable, the management committee. In practice, however, this is very often the case and is recommended by the NBB. The CFO is generally responsible for managing financial resources, financial planning and financial reporting. In firms where the CFO is not a senior manager or, where applicable, a member of the management committee, the CFO should be a senior member of staff (at N-1 level in relation to the senior managers).

Chief risk officer

4:49 Pursuant to Article 33 §3 of the Brokerage Supervision Act, the person responsible for the risk management function (usually referred to as the chief risk officer or CRO) must be a member of senior management or, where applicable, the management committee. In principle, this person should only be responsible for the risk management function. However, by way of derogation from this rule, the NBB may authorise the CRO to be responsible for the compliance function as well, provided these two functions are performed separately.

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[28] A derogation allowing a mixed management committee in terms of composition (directors and non-directors) is, however, possible on the basis of Article 22 of the Brokerage Supervision Act.

[29] See Article 64 of the Brokerage Supervision Act. Thus, the person to whom daily management has been delegated (for corporate forms where this possibility exists) must be an executive director with self-employed status.

[30] A subordinate relationship - if proven - would compromise the proper functioning and collective decision-making of senior management.

4:50 Furthermore, the NBB may allow the risk management function - taking into account the principle of proportionality - to be exercised by a senior member of staff (at N-1 level in relation to senior management), provided there is no conflict of interest on the part of this person. Small stockbroking firms may also request this derogation.

Senior manager responsible for the prevention of money laundering and countering the financing of terrorism (AML/CFT)

4:51 In accordance with Article 9 §1 of the Act of 18 September 2017 on the prevention of money laundering and terrorist financing and on restriction of the use of cash, the firm must appoint a senior manager responsible for AML/CFT from amongst the members of its senior management or, where applicable, its management committee. The senior manager responsible for AML/CFT is expected to possess general AML/CFT-related knowledge so as to be able to review critically the measures taken by the AMLCO and ensure compliance with the provisions of AML Act. It should also be ensured that the senior manager responsible for AML/CFT does not combine this role with other roles giving rise to AML/CFT risks (such as a commercial function).

4.1.3.2. Tasks

4:52 In accordance with, in particular, Article 59 of the Brokerage Supervision Act, senior managers or, where applicable, members of the management committee are entrusted with the following tasks:

a) managing the firm's business and developing its management structure;
b) supervising line management, monitoring compliance with assigned powers and responsibilities, and overseeing financial reporting;
c) making suggestions to and advising the statutory governing body with regard to determination of the firm's general policy and strategy and providing all relevant information and data to enable the statutory governing body to take informed decisions;
d) organising, steering and assessing the internal control mechanisms and procedures, in particular as regards the independent control functions, without prejudice to supervision carried out by the statutory governing body;
e) ensuring that the remuneration policy established by the statutory governing body is correctly implemented;
f) implementing the necessary measures to ensure proper risk management, including in particular providing the statutory governing body with appropriate information on all significant risks, management policies and the management of significant risks;
g) organising an internal control system that provides reasonable assurance on the reliability of internal reporting and financial disclosure, in order to ensure that the annual accounts are in compliance with the applicable accounting rules and regulations;
h) reporting to the statutory governing body on the firm's financial position, the effectiveness of the internal control system and all aspects necessary to fulfil its tasks correctly.

4:53 With regard to the last point, Article 59 of the Brokerage Supervision Act provides that the management committee should report at least every two years (depending on the size of the firm) to the statutory governing body, the certified auditor and the NBB on its assessment of the effectiveness of the organisational requirements imposed by the Brokerage Supervision Act and on any measures taken to remedy the identified shortcomings.[31]

4:54 Furthermore, senior management should confirm to the NBB every six months that the periodic reports comply with the accounts and inventories ("statement on periodic prudential reporting"). A copy of this statement must be provided to the statutory governing body and the certified auditor.

[31] As specified in Circular NBB_2011_09, the management committee must submit two reports in this respect: an assessment report on the internal control system and an assessment report on the internal controls as regards investment services and activities.

4:55 For more information on the tasks of senior management (or, where applicable, the management committee), please see paragraphs 32 to 35 of EBA/GL/2021/14.

4.1.3.3. Functioning

4:56 Senior management forms a body that takes decisions collectively - preferably unanimously, otherwise by a majority - with the senior managers exercising effective reciprocal supervision.[32] Where a management committee has been set up, it is a collective decision-making body.

4:57 Collective decision-making does not, however, preclude the allocation of specific tasks or responsibilities to members of senior management or, where applicable, the management committee. In this respect, it is recommended that the internal division of tasks between senior management (or, where applicable, members of the management committee) comply with the following two principles: (i) there should be a strict separation between "risk management" and "investment" functions as well as between "risk management" and "commercial" functions and (ii) the internal audit should be assigned to a member of the management committee who is not otherwise responsible for a "commercial" function.

4:58 The division of tasks between the members of senior management or, where applicable, the management committee must be notified to the NBB in accordance with Article 61 §3 of the Brokerage Supervision Act and be set out in the governance memorandum. Material changes to this division of tasks are subject to the prior approval of the NBB.[33]

4:59 Decisions are taken by senior management or, where applicable, the management committee by consensus[34] and set down in minutes, with all members faithfully obliged to comply with them. The minutes of meetings should summarise the discussions held, record the decisions taken, and specify the differing views expressed by members, in accordance with the provisions of the Corporate Governance Code published by royal decree on 12 May 2019.

4:60 It is recommended that senior management or, where applicable, the management committee adopt by-laws[35] describing its composition, tasks and functioning and which comply in particular with Article 59/1 of the Brokerage Supervision Act with regard to the management of conflicts of interest. The NBB recommends that these by-laws be appended to the governance memorandum.

4:61 Senior management or, where applicable, the management committee should meet regularly.

4:62 For the rules on induction and training, please see the section on the statutory governing body above and the NBB's Fit & Proper Manual.

4.1.3.4. Derogations

4:63 Pursuant to Article 22 of the Brokerage Supervision Act, based on the size and risk profile of the firm, the NBB may authorise a derogation from the requirement that all members of the management committee be directors and the prohibition on combining the roles of management committee member and chair of the statutory governing body. In this case, a detailed file justifying the request for an exemption must be submitted to the NBB.

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[32] There should be a clear legal framework for any delegation of powers relating to day-to-day management (e.g. the articles of association).

[33] See footnote 129 to the NBB's Fit and Proper Manual.

[34] If senior management or, where applicable, the management committee consists of just two persons, mechanisms to avoid deadlock in the decision-making process should be put in place.

[35] These by-laws do not necessarily have to meet the conditions set out in Article 2:59 CAC.

4.1.4. SPECIALISED COMMITTEES

Statutory and regulatory framework

1. Brokerage Supervision Act: Articles 23 to 30
2. NBB circulars:
   - Communication NBB_2022_34 of 22 December 2022 updating the NBB's Fit & Proper Manual
   - Circular NBB_2021_27 transposing EBA/GL/2021/06 on the assessment of suitability
   - Circular NBB_2021_30 of 7 December 2021 on remuneration policies: update of the legal framework and transposition of EBA/GL/2021/04 on sound remuneration policies under Directive 2021/36/EU
   - Communication CBFA_2009_22 of 25 May 2009 on the derogation policy for audit committees
3. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 44 to 60

4.1.4.1. General information

4:64 Where necessary, the statutory governing body should set up specialised committees to analyse specific issues and advise it thereon. The creation of such committees may not undermine the role of the statutory governing body: decisions are always taken by the statutory governing body, which exercises its powers as a collective.

4:65 In order to enhance the effectiveness of oversight and supervision of the firm's activities, operations and risk profile by the statutory governing body, Article 24 of the Brokerage Supervision Act provides that two specialised committees should be set up within this body:[36]

- a risk committee and
- a remuneration committee.

4:66 When the NBB finds that a firm is significant in terms of its size, internal organisation or the nature, scale and complexity of its activities, it may request, pursuant to Article 24 §2 of the Brokerage Supervision Act, the establishment of audit and nomination committees or a single committee to carry out the tasks assigned to the audit and risk committees and/or a single committee that carries out the tasks assigned to the remuneration and nomination committees.[37] If the NBB does not exercise this prerogative, the functions assigned to the audit committee shall be exercised by the risk committee[38] while those assigned to the nomination committee shall be exercised by the remuneration committee.

4:67 A stockbroking firm may also establish an audit committee on a voluntary basis.[39]

4.1.4.2. Composition

4:68 The committees to be set up pursuant to Article 24 of the Brokerage Supervision Act must be comprised exclusively of non-executive directors serving on the statutory governing body and at least one independent member within the meaning of Article 3(64) of the Brokerage Supervision Act.

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[36] Except for small stockbroking firms which are exempt pursuant to Article 25 of the Brokerage Supervision Act (see Section 4.1.4.4 of this manual).

[37] The option for the NBB to require the establishment of an audit committee and a nomination committee or an audit and risk committee and/or a nomination and remuneration committee does not apply to small stockbroking firms (unlike the option to require the creation of a management committee).

[38] For example, monitoring the work of the internal audit function and monitoring the statutory audit of the accounts and the recommendations made by the statutory auditor fall within the tasks of the risk committee.

[39] If a stockbroking firm creates an audit committee and/or a nomination committee, either voluntarily or at the request of the NBB, the rules governing the composition and tasks of these committees are those set out in Article 7:99 §4 CAC, to which Article 26 of the Brokerage Supervision Act refers, for the audit committee and/or those set out in Article 31 of the Brokerage Supervision Act, for the nomination committee. The procedural rules set out in this manual also apply to these committees.

4:69 Pursuant to Article 24 §3 of the Brokerage Supervision Act, stockbroking firms must ensure that the same member does not serve on more than three committees.

4:70 In accordance with paragraph 53 of EBA/GL/2021/14, the following measures contribute to the proper functioning of the committees and are therefore – without prejudice to stricter requirements provided for by the CAC[40] - recommended good practices:

- the chair of the risk committee should not also chair the statutory governing body or any other committee; and
- the chair of the risk committee should be independent within the meaning of Article 3(64) of the Brokerage Supervision Act.

4:71 Where specialised committees must be set up in accordance with Article 24 of the Brokerage Supervision Act, their members should have the specific expertise described in Articles 26 to 29 of this act.

4:72 In the performance of its prudential supervisory tasks, the NBB should assess the knowledge and experience of prospective members of the aforementioned committees and examine whether the composition and procedures of these committees offer sufficient guarantees to enable them to carry out their duties properly.[41]

4.1.4.2. Tasks

4.1.4.2.1. Risk committee

4:73 The duties of the risk committee are set out in Article 27 of the Brokerage Supervision Act and further specified in EBA/GL/2021/14. Thus, the risk committee should at least:

a) advise and support the statutory governing body in its supervisory function with regard to monitoring of the firm's overall current and future risk strategy and appetite;
b) assist the statutory governing body in the exercise of its supervisory function and particularly the non-executive directors in overseeing implementation of the firm's risk strategy and the corresponding limits that have been set;
c) oversee implementation of the firm's strategies for capital and liquidity management as well as for all other relevant risks;
d) provide the statutory governing body, in its supervisory capacity and particularly the non-executive directors, with recommendations on necessary adjustments to the risk strategy;
e) advise on the selection of any external consultants the supervisory function may decide to engage for advice or support;
f) review various possible scenarios, including stressed scenarios, to assess how the firm's risk profile would react to external and internal events;
g) oversee the alignment between all material financial instruments offered to customers and the business model and risk strategy of the firm;
h) evaluate the recommendations of the risk management and compliance functions as well as, in the absence of an audit committee, those of the internal audit function and the statutory auditor and monitor the appropriate implementation of the measures taken;
i) ensure that the services offered to customers take into account the risks incurred by the firm in view of its business model and risk strategy, in particular those - especially reputational risks - that could arise based on the types of products offered to customers; where this is not the case, the risk committee should provide an action plan to the statutory governing body; and

[40] Article 30 of the Brokerage Supervision Act provides that Articles 24, 26 and 28 are without prejudice to the provisions of the CAC relating to the audit committee and the remuneration committee in listed companies within the meaning of Article 1:11 CAC.

[41] In this context, it should be ensured that the committees are not too small so as to avoid deadlock when a member is absent.

j) assess whether the incentives in terms of variable remuneration take suitable account of the firm's risk management, capital requirements and liquidity position, as well as the probability and staggering of profits.

4:74 For more information, please see paragraphs 59 and 60 of EBA/GL/2021/14.

4.1.4.2.2. Remuneration committee

4:75 The duties of the remuneration committee are set out in Article 28 of the Brokerage Supervision Act. This committee must at least:

a) issue an opinion on the firm's remuneration policy and any changes made thereto. In this respect, the remuneration committee must in particular examine whether the incentives created by the remuneration policy, including the promotion system, are not such as to encourage excessive risk-taking within the firm or promote behaviour that pursues interests other than those of the firm and its stakeholders. It must also ensure that the remuneration policy does not give rise to conflicts of interest, in particular to the detriment of customers to whom certain services are offered;
b) prepare decisions concerning remuneration that have consequences for the firm's risks and risk management and on which the statutory governing body must decide; and
c) ensure direct supervision of the remuneration allocated to the heads of independent control functions.

4:76 Furthermore, the remuneration committee may rely on information provided by the risk committee to propose changes to the decisions of the statutory governing body relating to variable remuneration.

4.1.4.3. Functioning

4:77 Members of specialised committees should engage in open and critical discussions, during which dissenting views are discussed in a constructive manner.

4:78 Committees should document the agendas of their meetings, their discussions, the conclusions of their work and their proposals for decisions to be submitted to the statutory governing body which should reflect the diverging views expressed by members. The conclusions and proposed decisions should be provided to the statutory governing body.

4:79 The statutory governing body establishes by-laws for each committee,[42] specifying its tasks, composition and functioning (including the drawing up of minutes). The NBB recommends that these by-laws be appended to the governance memorandum.

4:80 Depending on their powers, committee members should at least:

a. have access to all relevant information and data necessary to perform their role, including information and data from relevant corporate and independent control functions (e.g. legal, finance, human resources, IT, internal audit, risk management, compliance, including information on AML/CFT compliance and aggregated information on suspicious transaction reports, and ML/FT risk factors);
b. receive regular reports, ad hoc information, communications and opinions from the heads of independent control functions concerning the firm's current risk profile, risk culture and risk limits, as well as on any material breaches that may have occurred, with detailed information on and recommendations for corrective measures taken, to be taken or suggested to address these breaches, and periodically review and decide on the content, format and frequency of the risk-related information reported to them; and
c. where necessary, ensure the proper involvement of the independent control functions and other relevant functions (human resources, legal, finance) within their respective areas of expertise and/or seek external expert advice.

[42] These by-laws do not necessarily have to meet the conditions set out in Article 2:59 CAC.

4:81 The committees should interact with each other as appropriate. To a limited extent, such interaction may take the form of cross-participation, meaning the chair or a member of a committee may also be a member of another committee.

4:82 For reasons of efficiency, external persons (e.g. the chair or a senior manager, the internal auditor, the statutory auditor) may attend all or some committee meetings in an advisory capacity. Nevertheless, the systematic attendance by non-members (executive directors, non-executive directors who are not members of the committee, group representatives, etc.) of specialised committee meetings should be avoided, except in duly justified cases. It is good practice to ensure that non-members take part only in discussions that are relevant to them and that at least one meeting per year is held without any non-members present. The committee chairs play an important role in ensuring the quality of the discussions.

4.1.4.4. Derogations for small stockbroking firms

4:83 Application of the statutory obligation to set up risk and remuneration committees within the statutory governing body, composed exclusively of non-executive directors and with at least one independent member within the meaning of Article 3(64) of the Brokerage Supervision Act, is not justified for small stockbroking firms. Thus, small stockbroking firms are exempt from the requirement to set up risk and remuneration committees and cannot be obliged to set up an audit committee or a nomination committee.

4:84 In the absence of committees, the statutory governing body as a whole is responsible for exercising the functions assigned to the various committees.[43]

4.1.4.5. Group context

4:85 Article 24 §4 of the Brokerage Supervision Act authorises the NBB to take into account the group context when allowing a stockbroking firm, where appropriate, not to set up one or more of the committees that are required by law. In this case, one or more committees that meet the requirements of the Brokerage Supervision Act should be set up within the group or subgroup concerned and entrusted with responsibility for the stockbroking firm.

4:86 Communication CBFA_2009_22 on audit committees applies *mutatis mutandis* to the derogation policy concerning the establishment of these other committees, it being understood that the specific tasks of each committee should be taken into account.

[43] As set out in Article 25 §2 of the Brokerage Supervision Act, when, further to a derogation granted in accordance with Article 22, the chair of the statutory governing body is an executive director, this person may not preside over the statutory governing body when the latter is carrying out the tasks assigned to the committees referred to in Article 24 of the Act.

4.2. ORGANISATIONAL SET-UP

4.2.1. ORGANISATIONAL FRAMEWORK AND STRUCTURE

Statutory and regulatory framework

1. Brokerage Supervision Act: Article 17
2. NBB regulations:
    - Regulation of 19 May 2015 on the internal control system and the internal audit function
3. NBB circulars:
    - Circular NBB_2021_17 of 6 July 2021 on prevention policy for tax matters
    - Circular NBB_2021_17 of 6 July 2021 on special mechanisms
    - Circular NBB_2015_21 on the internal control system and the internal audit function
4. International reference documents:
    - EBA/GL/2021/14 on internal governance => paragraphs 61 to 84

4.2.1.1 Organisational framework

4:87 The statutory governing body should implement and ensure a suitable and transparent organisational and operational structure for the firm. This implies in particular that the reporting lines and the division of responsibilities should be clear, well defined, coherent and adequately documented. For more information on this subject, please see paragraphs 61 to 64 of EBA/GL/2021/14.

4.2.1.2. Decision-making process, reporting lines and division of tasks

4:88 The firm should have a clear, transparent and documented decision-making process and a clear division of responsibilities and reporting lines within its internal control framework, covering its business lines, internal units and independent control functions.

4:89 Reporting lines should be clearly defined. Internal reporting should be adapted to the nature, size, complexity and risk profile of the firm and should cover all of the firm's activities.

4:90 When implementing the internal control framework, firms should ensure an adequate segregation of duties, for example by allocating conflicting activities or supervisory and reporting responsibilities to different persons and by establishing information barriers to prevent the transmission of certain information (e.g. through the physical separation of certain departments).

4.2.1.3. Administrative and accounting organisation

4:91 The firm should have an appropriate administrative and accounting organisation, including inter alia a system of controls that provides a reasonable level of assurance of the reliability of the financial reporting process.

4:92 Senior management or, where applicable, the management committee must take, under the supervision of the statutory governing body, the necessary steps to ensure that the firm has reliable financial and prudential reporting.

4.2.1.4. Know your structure

4:93 Directors should have a clear understanding of the firm's legal and operational structure and of its activities, including the risks associated with the services and products offered. They must ensure that this structure and these activities are in line with the approved business and risk strategy and risk appetite. Support functions (secretary general, legal affairs, human resources, communication) and the independent control functions should be given all specific information they need to fulfil their respective tasks properly.

4:94 Firms that are part of a group should be able to inform the NBB of the structure of the group to which they belong, as well as the group's governance and the control mechanisms applicable to them. When a firm has a large number of legal entities within its group, their number, and in particular any links and transactions between them, should not constitute an obstacle to sound governance or efficient management and supervision of the group's risks.

4:31 For more information, please see paragraphs 65 to 69 of EBA/GL/2021/14.

4.2.1.5. Complex structures and non-standard or non-transparent activities

4:96 Firms may develop cross-border activities. The decision to develop activities in foreign jurisdictions may be driven by a range of factors and circumstances relating to legitimate strategic, commercial or financial objectives. However, complex structures or foreign activities, in particular in offshore financial centres or non-transparent jurisdictions, may give rise to financial, legal and/or reputational risks and thus may not meet prudential requirements.

4:97 For more information on this subject, please see paragraphs 70 to 76 of EBA/GL/2021/14. In addition, please refer to the provisions on special mechanisms and prevention policy for tax matters which have recently been revised (see in particular Article 17 §2 of the Brokerage Supervision Act and Circulars NBB_2021_17 of 6 July 2021 on prevention policy for tax matters and NBB_2021_17 of 6 July 2021 on special mechanisms).

4.2.2. OUTSOURCING

Statutory and regulatory framework

1. Brokerage Supervision Act: Articles 17 and 73
2. NBB circulars:
   - Circular NBB_2019_19 on the European Banking Authority (EBA) Guidelines on outsourcing arrangements of 25 February 2019 (EBA/GL/2019/02)
3. International reference documents:
   - EBA/GL/2019/02 on outsourcing

4:98 In accordance with Article 17 of the Brokerage Supervision Act, a firm must have an appropriate monitoring system to ensure its effective and prudent management.

4:99 Article 73 of the Brokerage Supervision Act moreover specifies that, in this context, firms are required to take appropriate measures to, on the one hand, limit the operational risk associated with outsourcing and, on the other hand, to ensure that the adequacy of their internal control procedures is not materially impaired and that the NBB is not prevented from monitoring the firm's compliance with the applicable statutory and regulatory requirements.

4:100 The prudential expectations on outsourcing are laid down in Circular NBB_2019_19. Please refer to this circular for more information on this subject.

4.2.3. HEAD OFFICE IN BELGIUM

Statutory and regulatory framework

1. Brokerage Supervision Act: Article 42

4:101 Article 42 of the Brokerage Supervision Act stipulates that, in order to obtain a licence, the head office of a stockbroking firm governed by Belgian law must must be established in Belgium, i.e. in the same Member

State as its registered office. This obligation stems from Directive 95/26/EC of 29 June 1995 (the "Post-BCCI Directive").[44]

4:102 The term "head office" should be understood within the meaning of Article 54 TFEU (ex Article 48 TEC) and covers the concept of "real seat", i.e. the place where essential decisions are taken and where the conduct of the firm's business is effectively concentrated. In order to conclude that the "nerve centre" of a firm with a cross-border structure is established in Belgium, it is recommended that all heads of independent control functions appear in the firm's personnel register and that a majority of meetings of the statutory governing body and senior management be held on the Belgian territory, at the firm's registered office.

[44] European Parliament and Council Directive 95/26/EC of 29 June 1995 amending Directives 77/780/EEC and 89/646/EEC in the field of credit institutions, Directives 73/239/EEC and 92/49/EEC in the field of non- life insurance, Directives 79/267/EEC and 92/96/EEC in the field of life assurance, Directive 93/22/EEC in the field of investment firms and Directive 85/611/EEC in the field of undertakings for collective investment in transferable securities (UCITS), with a view to reinforcing prudential supervision.

4.3. RISK CULTURE AND INTEGRITY

4:103 Sound governance cannot be achieved through management and organisational structures, procedures and control mechanisms alone; it depends to a large extent on the commitment and dedication of all staff members and the existence of a suitable corporate culture.

4.3.1. RISK CULTURE

Statutory and regulatory framework

1. Brokerage Supervision Act: Article 17
2. NBB circulars:
/
3. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 85 to 89

4:104 A sound, diligent and consistent risk culture should be a key element of effective risk management by stockbroking firms and enable them to take sound and informed decisions. A sound risk culture includes, but is not necessarily limited to, “tone at the top”, diversity and inclusion, accountability, an environment of open communication and effective challenge, and the absence of risk-taking incentives. The risk management function and the compliance function should play an active role in implementing a sound risk culture. For more information on this subject, please see paragraphs 85 to 89 of EBA/GL/2021/14.

4.3.2. CORPORATE VALUES AND CODE OF CONDUCT

Statutory and regulatory framework

1. Brokerage Supervision Act: Articles 17 §1(5) and 19, second paragraph, (4)
2. NBB circulars:
/
3. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 90 to 95

4:105 The statutory governing body should develop, adopt, adhere to and promote high ethical and professional standards, taking into account the specific needs and characteristics of the firm, and should ensure the implementation of such standards through a code of conduct or similar instrument.
For more information on this subject, please see paragraphs 90 to 95 of EBA/GL/2021/14.

4.3.3. REMUNERATION

Statutory and regulatory framework

1. Brokerage Supervision Act: Article 17 §1(6), 74 to 79 and the Annex
2. European and Belgian regulations:
   - EBA/RTS/2021/01 of 21 January 2021 on classes of instruments that adequately reflect the credit quality of the investment firm as a going concern and possible alternative arrangements that are appropriate to be used for the purposes of variable remuneration
   - EBA/RTS/2021/02 of 21 January 2021 on criteria to identify categories of staff whose professional activities have a material impact on an investment firm's risk profile or assets it manages under Directive (EU) 2019/2034 (IFD) of the European Parliament and of the Council on the prudential supervision of investment firms
   - Regulation of the NBB of 1 April 2014 on proprietary trading activities

3. NBB circulars:
    - See Annex 3 to this manual transposing EBA/GL/2021/13 of 22 November 2021 on sound remuneration policies under Directive (EU) 2019/2034
    - Circular NBB_2022_29 of 17 November 2022 transposing the EBA Guidelines of 30 June 2022 on the data collection exercise on high earners under the CRD and the IFD (EBA/GL/2022/08)
    - Circular NBB_2022_28 of 17 November 2022 transposing the EBA Guidelines of 30 June 2022 on remuneration and gender pay gap benchmarking under the CRD and the IFD (EBA/GL/2022/07)
    - Communication NBB_2024_02/NBB on the cross-sectional analysis of remuneration policies and practices of credit institutions – findings and recommendations
4. International reference documents:
    - EBA/GL/2021/13 of 22 November 2021 on sound remuneration policies for investment firms under Directive (EU) 2019/2034 (Annex 3 to this manual)

4:106 The statutory governing body should develop a remuneration policy aimed at ensuring that the personal objectives of staff members are aligned with the long-term interests of the firm. To this end, the firm should establish and maintain a remuneration policy and remuneration practices that promote effective risk management.

4.3.3.1. *Identified Staff*

4:107 Firms must identify the members of staff to whom specific requirements on remuneration apply ("identified staff"). These include in particular the categories of staff whose professional activities have a material impact on the firm's risk profile.

4:108 This identification process must be carried out on the basis of the criteria set out in EBA/RTS/2021/02. In addition, pursuant to Article 9 §2 of the NBB Regulation of 1 April 2014, all staff members who are authorised to perform high-risk transactions and are employed in trading departments should in any case be considered identified staff.

4:109 The NBB recommends that at least 1% of all staff members be considered identified staff.

4.3.3.2. EBA Guidelines

4:110 According to Article 39(9) IFD, the EBA must issue guidelines on sound remuneration policies which comply with the principles set out in Articles 30 to 33 IFD. The latest version of these guidelines was published on 22 November 2021. This manual transposes EBA/GL/2021/13 into Belgian law.

4:111 These guidelines will assist the NBB in its monitoring of firms' remuneration policies and practices.[45] They complete and clarify the regulatory framework to be complied with by stockbroking firms.

4:112 New aspects of EBA/GL/2021/13 include transparency to stakeholders, proportionality, the need for a gender-neutral remuneration policy and monitoring of the gender pay gap.

4.3.3.3. Variable remuneration - same cap as that applicable to banks

4:113 The IFD requires the Member States to ensure that firms set appropriate ratios between the variable and fixed components of total remuneration in their remuneration policy, taking into account the firm's commercial activities (and the associated risks) and the impact that the relevant categories of staff have on its risk profile.

[45] The entry into force of the CAC had very limited impact on the remuneration rules. Listed institutions must now ensure that their remuneration policies comply with Article 7:92, fourth paragraph, last sentence of the CAC, which stipulates that no variable remuneration may be awarded to an independent director. In addition, the CAC provides for the possibility for the general meeting to grant a notice period and severance pay to directors, as the principle that directors may be removed "at will" is no longer mandatory.

4:114 However, Recital 25 to the IFD specifies that the Member States may adopt stricter national requirements concerning the maximum ratio between the variable and fixed components of remuneration or even impose such a ratio on all investment firms (or certain ones).

4:115 Belgium has exercised the option (explicitly) provided for by the IFD and maintained the cap on the variable component of remuneration at a level similar to that applicable to credit institutions, i.e. the higher of the two following amounts (i) 50% of the fixed component of remuneration or (ii) €50,000 provided this amount does not exceed the fixed component of remuneration.

4:116 Maintaining this cap allows for a level playing field with banking groups that also engage in investment activities.

4.3.3.4. Financial instruments

4:117 The NBB expects firms to comply with the requirement set out in the Annex to the Brokerage Supervision Act, pursuant to which at least 50% of all variable remuneration must be appropriately balanced between shares or equivalent instruments and, if possible, other capital instruments mentioned in the act. The conditions under which the aforementioned capital instruments can be used for variable remuneration are listed in EBA/RTS/2021/01.

4.3.3.5. Termination and severance payments

4:118 In line with the IFD and EBA/GL/2021/13, the Annex to the Brokerage Supervision Act specifies the rules applicable to termination payments, including severance payments.

4:119 In general, termination payments always constitute variable remuneration. Therefore, such payments should be subject to the rules applicable to variable remuneration.

4:120 However, the Annex to the Brokerage Supervision Act and the aforementioned EBA Guidelines provide for a limited number of exhaustively listed situations in which severance pay (or a portion thereof) may be excluded for the purpose of (i) calculating the ratio of fixed to variable remuneration and (ii) applying the rules on deferral and payment in instruments.

4.3.3.6. Collection of data on remuneration

4:121 Pursuant to Article 450 of Regulation No 575/2013, firms must disclose certain quantitative information on their remuneration policies and practices. The NBB uses the information so collected to benchmark remuneration trends and practices. Firms selected by the NBB for this purpose should report on an annual basis, pursuant to Circular NBB_2022_28.

4:122 Furthermore, pursuant to Article 22 of the Annex to the Brokerage Supervision Act, firms should provide the NBB with information on the number of natural persons within the firm that receive remuneration of at least €1 million per financial year, broken down into tranches of €1 million, along with information on their professional responsibilities, the area of activity concerned, and the primary components of their remuneration, including bonuses, long-term benefits and pension contributions. The reporting methods are specified in Circular NBB_2022_29.

4.3.4. CONFLICTS OF INTEREST

Statutory and regulatory framework

1. Brokerage Supervision Act: Articles 17 §1(3), 38, 62, 63 and 83 to 84
2. NBB regulations:
   - Royal Decree of 8 February 2022 approving the NBB Regulation of 9 November 2021 on the exercise of external functions by managers and heads of independent control functions of regulated entities
3. NBB circulars:
   - Communication NBB_2022_34 of 22 December 2022 updating the NBB's Fit & Proper Manual
   - Communication NBB_2022_19 of 12 July 2022 on the exercise of external functions by managers and heads of independent control functions of regulated entities
   - Circular NBB_2021_27 transposing EBA/GL/2021/06 on the assessment of suitability
   - Circular NBB_2017_21 of 7 July 2017 on loans, credit and guarantees granted to managers, shareholders and related persons
4. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 105 to 131
   - EBA/GL/2021/06 on the assessment of suitability

4:123 The activity of a stockbroking firm is characterised by a variety of interests - often converging but just as often diverging or competing - which require appropriate rules.

4:124 Conflicts of interest may arise in the following relationships (non-exhaustive list):

- between shareholders and the firm;
- between directors and the firm;
- between staff and the firm and, by extension, the firm's customers;
- between the firm and its customers, as a result of the business model implemented and/or the services and activities offered by the firm;
- between customers;
- between the firm and its parent undertaking, a subsidiary or other affiliated undertaking, in the context of intra-group transactions.

4:125 Without prejudice to application of the provisions of the Companies and Associations Code or other applicable rules (investment services, market abuse), two types of conflicts of interest policies should be developed.

4.3.4.1. Conflicts of interest policy at firm level

4:126 The statutory governing body is responsible for establishing, approving and overseeing the implementation and maintenance of effective policies to identify, assess, manage and mitigate or prevent actual and potential conflicts of interest at firm level, e.g. as a result of the various activities and roles of the firm, of different firms within the consolidated scope of prudential supervision or of different business lines or units within the firm, or with regard to external stakeholders (including, where appropriate, entities in which a director of the firm holds a position).

4:127 For more information on the conflicts of interest policy at firm level, please see paragraphs 96 and 97 of EBA/GL/2021/14.

4.3.4.2. Conflicts of interest policy for staff

4:128 The statutory governing body is responsible for establishing, approving and overseeing the implementation and maintenance of effective policies to identify, assess, manage and mitigate or prevent actual and potential conflicts between the interests of the firm and the individual interests of staff, including members of the statutory governing body, which could adversely influence the performance of their duties and responsibilities and the firm's activities.

4:129 The conflicts of interest policy for staff should aim to identify conflicts of interest on the part of staff, including the interests of their closest family members.

4:130 For more information on the conflicts of interest policy for staff, please see paragraphs 98 to 119 of EBA/GL/2021/14.

4:131 The EBA Guidelines also contain a series of recommendations regarding "loans and other transactions with members of the management body and their related parties". These provisions should be read in conjunction with Article 83 of the Brokerage Supervision Act and Circular NBB_2017_21, which govern the granting of loans, credit and guarantees to members of the statutory governing body and their related parties. Please see paragraph 3.3 of this manual for more information on this subject.

4.3.4.3. General measures applicable to all types of conflicts of interest

4:132 The measures taken by the firm to manage or, as the case may be, mitigate conflicts of interest should be documented. This process should include the following measures and procedures:

- establishing information barriers or ensuring the physical separation of certain departments with regard to IT matters;
- entrusting conflicting activities within a chain of transactions or services to different persons;
- entrusting supervisory and reporting responsibilities relating to (potentially) conflicting activities to different persons;
- avoiding a direct link between the remuneration of the relevant persons and the revenue generated by conflicting activities;
- avoiding situations in which persons from within or outside the firm with a conflict of interest can exercise inappropriate influence over the firm's activity;
- establishing appropriate policies and procedures for transactions with related parties. This could include requiring, for example, that transactions be conducted at arm's length terms, that a binding opinion be given by independent members of the statutory governing body, that exposure to such transactions be limited, etc.;
- providing that the members of the statutory governing body have a responsibility to abstain from voting on matters in which they have or may have a conflict of interest or where the objectivity or ability of the person concerned to perform the duties properly could be compromised;
- limiting the external activities of the persons concerned.

4:133 It is good practice to inform interested stakeholders of the general nature and sources of conflicts of interest and of the policy applied by the firm to identify, prevent and manage these conflicts. For more information on this subject, please see EBA/GL/2021/14, the NBB's Fit & Proper Manual, the NBB Regulation and Communication NBB_2022_19 on external functions, and Circular NBB_2017_21 on loans to managers.

4.3.5. INTERNAL AND EXTERNAL REPORTING OF BREACHES (WHISTLEBLOWING)

Statutory and regulatory framework

1. Brokerage Supervision Act: Articles 17 §1(8) (internal reporting of breaches)
2. Other legislation:
   - Act of 22 February 1998 establishing the organic statute of the National Bank of Belgium: Article 36/7/1 (external reporting of breaches)
   - Act of 28 November 2022 on the protection of persons who report breaches of Union law or national law within a legal entity in the private sector (transposing Directive (EU) 2019/1937 of the European Parliament and of the Council of 23 October 2019 on the protection of persons who report breaches of Union law, which governs the establishment of internal and external reporting channels and the handling of breach reports)
3. NBB circulars: /
4. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 120 to 128

4.3.5.1. Internal reporting of breaches

4:134 Compliance with legislation, corporate values and the codes of conduct applicable to stockbroking firms as well as the effectiveness of internal controls are enhanced where there are internal channels for staff to raise legitimate concerns, in good faith, regarding material breaches of such laws and regulations, corporate values and codes or regarding unethical or illegal behaviour concerning matters falling under the firm's authority and control. In this context, firms should put in place and maintain appropriate internal reporting policies and procedures for staff to report breaches or potential breaches of statutory, regulatory or internal requirements, including in particular those imposed by the Brokerage Supervision Act and Regulation (No) 575/2013, or of internal governance arrangements, through a specific, independent and autonomous channel.

4:135 For more information, please see paragraphs 120 to 126 of EBA/GL/2021/14 and the Act of 28 November 2022 transposing Directive (EU) 2019/1937 of the European Parliament and of the Council of 23 October 2019 on the protection of persons who report breaches of Union law.

4.3.5.2. External reporting of breaches

4:136 The NBB has set up an external channel to report breaches. Information on this system can be found on the NBB's website under "Report a breach".[46] Article 36/7/1 of the Act of 22 February 1998 establishing the organic statute of the National Bank of Belgium and the Act of 28 November 2022 transposing Directive (EU) 2019/1937 prohibit any civil, penal or disciplinary proceedings, any professional sanctions and any unfavourable or discriminatory treatment, as well as any termination of the employment contract of a staff member for reporting a breach. The NBB may impose an administrative sanction on any firm that violates this prohibition.

4:137 The NBB uses the information provided in these reports solely for the purpose of performing its legal duties. This information is subject to the heightened duty of confidentiality laid down in Article 36/7/1 §2 of the Act of 22 February 1998 establishing the organic statute of the National Bank of Belgium and the Act of 28 November 2022 transposing Directive (EU) 2019/1937. The protection of the reporting person and the person concerned is therefore guaranteed.

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46 It should be noted that the system for reporting breaches to the NBB is not intended to be used solely for violations of the Brokerage Supervision Act and extends to violations of other prudential legislation and anti-money laundering legislation.

4.3.6. PREVENTION OF MONEY-LAUNDERING AND TERRORIST FINANCING

Statutory and regulatory framework 1. Legislation: Article 17 §1(2) of the Brokerage Supervision Act and the Act of 18 September 2017 2. NBB regulations/circulars and international reference documents: Please see the dedicated section of the NBB's website.

4:138 The identification, management and mitigation of the risk of money laundering and terrorist financing should form an integral part of a firm's governance and risk management arrangements. For more information, please see the section of the NBB's website on the prevention of money laundering and terrorist financing (Combating money laundering and the financing of terrorism | nbb.be).

4.3.7. DIVERSITY

Statutory and regulatory framework 1. Legislation: Article 29 of the Brokerage Supervision Act

4:139 In order to ensure a sufficiently diverse pool of candidates for the statutory governing body, firms should put in place a diversity policy for staff that includes career planning aspects and measures to ensure equal treatment and opportunities for employees of all genders. In particular, these measures should ensure that the issue of appropriate gender representation is taken into account when selecting staff for managerial positions and providing management training.

4.4 INTERNAL CONTROLS AND THE INDEPENDENT CONTROL FUNCTION

4.4.1. INTERNAL CONTROL FRAMEWORK

Statutory and regulatory framework:

1. Brokerage Supervision Act: Article 17 §1(2)
2. NBB regulations:
   - Regulation of 19 May 2015 on the internal control system and the internal audit function
3. NBB circulars:
   - Uniform letter of 16 November 2015 on the assessment report of senior management on the internal control system
   - Circular NBB_2015_21 of 13 July 2015 on the internal control system and the internal audit function
   - Circular NBB_2011_09 of 20 December 2011 on the assessment report of senior management on the internal control system
4. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 129 to 138

4:140 Firms should develop and maintain a culture that encourages a positive attitude to risk management and compliance, as well a robust and comprehensive internal control framework.

4:141 The internal control framework should be adapted to the specificities and complexity of the firm's activities and the associated risks, taking into account the group context. Firms should organise the exchange of the necessary information in a manner that ensures that each management body, business line and internal unit, including each independent control function, is able to carry out its duties. This means, for example, that appropriate information should be exchanged between business lines and the compliance function (including the AMLCO), as well as between the heads of the independent control functions at group level and the firm's statutory governing body.

4:142 Firms should put in place, maintain and regularly update adequate internal control policies, processes/mechanisms and procedures. The expected level of sophistication of these policies, procedures and processes for small stockbroking firms is lower.

4:143 For more information on the internal control framework, please see paragraphs 129 to 138 of EBA/GL/2021/14.

4.4.2. RISK MANAGEMENT FRAMEWORK

Statutory and regulatory framework:

1. Brokerage Supervision Act: Article 17 and 68 to 73
2. NBB circulars: /
3. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 139 to 149

4:144 As part of their internal controls, firms should have a holistic, firm-wide risk management framework extending across all business lines and internal units, including independent control functions, one that fully recognises the economic substance of all risk exposures (including environmental and climate-related risks). The risk management framework should enable the firm to make fully informed decisions on risk-taking.

4:145 The risk management framework should also include, pursuant to Articles 68 to 72 of the Brokerage Supervision Act, the following measures related to the management of risks associated with the provision of investment services:

- a record of investment services, investment activities and transactions performed;
- measures to safeguard the rights of customers in order to prevent the use of customer funds for the firm's own behalf;
- accounting that allows assets held for a specific customer to be distinguished at any time and without delay from those held for other customers and from the firm's own assets;
- a process to validate financial instruments intended for retail sale, etc.

4:146 For more information on the risk management framework, please see paragraphs 139 to 149 of EBA/GL/2021/14.

4.4.4. INDEPENDENT CONTROL FUNCTIONS

Statutory and regulatory framework

1. Brokerage Supervision Act: Articles 31 to 36
2. NBB regulations:
   - Regulation of 19 May 2015 on the internal control system and the internal audit function (approved by the Royal Decree of 5 July 2015)
3. NBB circulars:
   - Communication NBB_2019_15 on the NBB's expectations regarding the content of the statutory governing body's assessment report on the compliance function
   - Circular NBB_2015_21 on the internal control system and the internal audit function
   - Circular NBB_2012_14 on the compliance function
4. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 150 to 201

4:147 Firms should set up three independent control functions:

- a risk management function;
- a compliance function; and
- an internal audit function.

4:148 These functions are necessary to enable the statutory governing body, in its supervisory capacity, to effectively oversee senior management.

4.4.4.1. GENERAL ASPECTS

4.4.4.1.1. Three lines of defence

4:149 The relations between, on the one hand, the commercial and business units, and, on the other, the independent control functions, are sometimes referred to as the three lines of defence model:

- the commercial and operational units (including the front office) are the firm's first line of defence, which is responsible for identifying the risks associated with each operation and observing the applicable procedures and limits;
- the second line of defence includes the risk management function and the compliance function, which are responsible for ensuring that risks are identified and managed by the operational units, in accordance with the applicable rules and procedures;
- the third line of defence is the internal audit, which, inter alia, monitors compliance with the applicable procedures by the first and second lines of defence.

4:150 The risk management, compliance and internal audit functions are necessary to ensure optimal performance of the supervisory role entrusted to the statutory governing body. They form a coherent group of cross-cutting control functions between which coordination is necessary. As these control functions are contiguous, they harmonise their activities and ensure an adequate exchange of relevant information. The risk management and compliance functions are supervised by the internal audit function.

4:151 None of the firm's areas of activity may, for personal, commercial or financial reasons, fall outside the scope of the control functions (e.g. offshore activities).

4:152 As regards the prevention of money laundering and terrorist financing (AML/CFT), the Anti-Money Laundering Act stipulates that firms should appoint one or more persons tasked with implementing and steering the AML/CFT policy (the "AMLCO"). For more information on this subject, please see the EBA Guidelines on the role and responsibilities of the AMLCO (EBA/GL/2022/05) and the NBB's website.[47]

4.4.4.1.2. Heads of independent control functions and the combining of control functions

4:153 The heads of the independent control functions should be at a hierarchical level that ensures they have the appropriate authority and stature needed to fulfil their responsibilities.

4:154 In general, the head of a control function should perform only this function, meaning it should not be combined with another control function (certainly not with an operational role or function). However, for small stockbroking firms and stockbroking firms that can justify a derogation from this rule based on the principle of proportionality, the NBB allows the same person to perform the risk management function and the compliance function provided (i) the performance of these two functions by the same person does not give rise to a conflict of interest (specifically, there is no "maker/checker" or "developer/inspector" situation), (ii) the person in question has the necessary knowledge and experience in both areas, and (iii) the person in question can devote the necessary time to the correct performance of both functions.

4.4.4.1.3. Independence of the control functions

4:155 The three control functions should be independent, which should at least be reflected in their status, their prerogatives, the arrangements for the remuneration of the heads of these functions and of the staff made available for the performance thereof, and their direct access to the statutory governing body (meaning they do not have to go through senior management). Notwithstanding the overall responsibility of the statutory governing body, the heads of the independent control functions should be independent from the business lines or units they oversee. Although the heads of the risk management, compliance and internal audit functions report to a member of senior management or, where applicable, the management committee,[48] they are directly accountable and answerable to the statutory governing body. Their performance is also reviewed by the latter.

4:156 For more information, please see paragraph 156 of EBA/GL/2021/14, which specifies the conditions control functions must meet in order to be considered independent.

4.4.4.1.4. Resources of the control functions

4:157 The independent control functions should dispose of sufficient (human and IT) resources to be able to carry out their tasks in an appropriate and independent manner. The heads of these functions should ensure that their staff possess the necessary qualifications and skills. For more information, please see paragraphs 157 and 158 of EBA/GL/2021/14.

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[47] Please see the section of the NBB's website on the prevention of money-laundering and terrorist financing.

[48] Functional reporting to a senior manager consists of reporting on the activities of the independent control function concerned, without that member being able to intervene in the decision-making process (no hierarchical role). The senior manager to whom the heads of the independent control functions report should also determine, in consultation with the statutory governing body and/or its specialised committees, the human and material resources (IT, etc.) required by the independent control function concerned to carry out its tasks properly and should monitor resource-related issues.

4.4.4.1.5. Methods and access

4:158 The methods and procedures used by the independent control functions should be commensurate with the nature, scale and complexity of the firm's activities and should be set down in writing.

4:159 The control functions should have access to all business lines and internal units with the potential to generate risk, as well as to relevant subsidiaries and affiliates. They should interact with the business units to help achieve the objective of firm-wide awareness of the importance of risk management.

4.4.4.1.6. Reporting

Regular reporting to the statutory governing body

4:160 The heads of the risk management, compliance and internal audit functions should report at least once a year directly to the statutory governing body on the performance of their tasks and also inform senior management (or, where applicable, the management committee). Such direct access, which implies they do not have to go through senior management, is necessary in order to enable the statutory governing body to exercise its supervisory function more closely with regard to implementation of the firm's strategy and its functioning.

4:161 Reporting to the statutory governing body can be done through the risk committee. When, in addition to the risk committee, an audit committee has also been set up, it is recommended that the risk management and compliance functions report to the risk committee and the internal audit function to the audit committee.[49]

4:162 The (at least) annual activity report of the independent control functions should:
1. document all tasks performed by the independent control function during the preceding period;
2. clearly indicate all shortcomings identified;
3. provide recommendations to remedy these shortcomings.

Own-initiative reports

4:163 Article 34 of the Brokerage Supervision Act provides that, when so justified by the circumstances, the heads of the risk management function and the compliance function can of their own initiative, without first referring the matter to senior management (or, where applicable, the management committee), inform the statutory governing body of their concerns and, where applicable, alert it to the fact that specific risk-related developments have or could have a negative impact on the firm or, in particular, could damage its reputation.

4.4.4.1.7. Periodic assessment

4:164 In the performance of its supervisory function, the statutory governing body should periodically, and at least once a year, verify the proper functioning of the independent control functions. To that end, it should regularly receive a report from senior management, without prejudice to the direct examination of any relevant information provided by the functions concerned, where applicable through the specialised committees set up for this purpose by the statutory governing body. For the compliance function, the statutory governing body should assess its functioning based on a predetermined model described in Circular NBB_2019_15 and should observe the collection date indicated in the NBB's communications on qualitative reporting.

4.4.4.1.8. Removal

4:165 In accordance with Article 62 §2 of the Brokerage Supervision Act, the heads of the independent control functions may not be removed without the prior approval of the statutory governing body acting in its

[49] Circular NBB_2019_15 stipulates that the compliance function reports to the statutory governing body through the audit committee. This reporting to the statutory governing body should now be understood as taking place, in most cases through the risk committee, although reporting through the audit committee may also be considered compliant.

supervisory capacity. If the removal of the head of an independent control function is being considered, the firm should first inform the NBB so that the latter can examine whether the reasons for removal are justified and, where appropriate, whether special measures should be taken based on the firm's governance.

4.4.4.2. COMPLIANCE FUNCTION

Statutory and regulatory framework

1. Brokerage Supervision Act: Articles 3, 33 and 34
2. NBB regulations:
   - Regulation of 6 February 2018 on the fitness of the responsible persons for the compliance function (approved by the Royal Decree of 15 April 2018)
   - Regulation of 27 October 2011 of the FSMA on the approval of compliance officers and the fitness of heads of the compliance function
3. NBB circulars:
   - Communication NBB_2019_29 on modification of the date for the transmission of compliance reports
   - Communication NBB_2019_15 on the NBB's expectations regarding the content of the statutory governing body's report on the assessment of the compliance function
   - Circular NBB_2012_14 of 4 December 2012 on the compliance function
4. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 183 to 190

4:166 Pursuant to Article 32 of the Brokerage Supervision Act, the compliance function is responsible for monitoring compliance with the statutory and regulatory provisions on integrity and conduct applicable to investment activities, investment services and/or ancillary services. The objective of the compliance function is thus to prevent the firm from suffering the consequences - in particular reputational damage, a loss of credibility or legal risks capable of causing serious financial harm - of non-compliance with the statutory and regulatory provisions or with the ethical rules applicable to asset managers (compliance risk). For more information on the compliance function, please see Circular NBB_2012_14 and paragraphs 183 to 190 of EBA/GL/2021/14.

4:167 The specific requirements regarding the expertise expected of the head of the compliance function are set out in the NBB's Regulation of 6 February 2018, while the conditions for authorisation by the FSMA are set out in the FSMA's Regulation of 27 October 2011. A new head of the compliance function is appointed in consultation between the NBB and the FSMA (if applicable, with a joint interview). This is the case even if a separate application must be sent to each authority. According to these regulations, the head of the compliance function should also, as from their appointment, undergo at least 40 hours of training every three years. Firms should also ensure that the other persons responsible for the compliance function participate in such a programme, with a minimum duration of 20 hours, every three years. The continuing training requirements are further explained in the explanatory note to the aforementioned regulation and Communication FSMA_2018_05 of 8 May 2018 on continuing training for compliance officers.

4:168 The statutory governing body should produce an annual report assessing the proper functioning of the compliance function.

4.4.4.3. RISK MANAGEMENT FUNCTION

Statutory and regulatory framework

1. Brokerage Supervision Act: Articles 33 and 34
2. NBB circulars: /
3. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 159 to 182

4:169 Pursuant to Article 33 §2 of the Brokerage Supervision Act, the risk management function ensures that all significant risks are detected, measured and duly reported. It should have access to all business lines and other internal units with the potential to generate risk, as well as to subsidiaries and affiliates. It should have an appropriate status and corresponding central position in the firm's organisational structure. The risk management function should be actively involved in developing the firm's risk strategy as well as in all management decisions with a significant impact in terms of risk and be able to provide a complete view of the entire range of risks to which the firm is exposed.

4:170 The tasks of the risk management function are described in detail in EBA/GL/2021/14. For more information on its role in (i) risk strategy and decisions, (ii) material changes, (iii) identifying, measuring, assessing, managing, mitigating, monitoring and reporting on risks, and (iv) risk limits, please see paragraphs 166 to 178 of EBA/GL/2021/14.

4:171 In accordance with Article 33 §3 of the Brokerage Supervision Act, the person responsible for the risk management function should in principle be a member of senior management or, where applicable, of the management committee. Moreover, the risk management function should be the sole function for which this person is responsible. However, based on the proportionality principle, the NBB may allow the risk management function to be exercised by a senior member of staff (N-1), provided there is no conflict of interest on the part of this person. Furthermore, Article 33 §3, second subparagraph, provides for a derogation from the principle that a CRO who is a member of senior management should be responsible only for the risk management function. The NBB may authorise a CRO who is a member of senior management to be responsible for the compliance function as well, provided these two functions are performed separately.

4:172 For more information, please see paragraphs 179 to 182 of EBA/GL/2021/14.

4.4.4.4. INTERNAL AUDIT FUNCTION

Statutory and regulatory framework

1. Brokerage Supervision Act: Article 35
2. NBB regulations:
   - Regulation of 19 May 2015 on the internal control system and the internal audit function
3. NBB circulars:
   - Circular NBB_2015_21 of 13 July 2015 on the internal control function and the internal audit function
4. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 191 to 201

4:173 An effective internal audit function provides, in an independent manner, reasonable assurance to the statutory governing body and senior management or, where applicable, the management committee as to the quality and effectiveness of the firm's internal control, risk management, and governance systems and processes.

4:174 The internal audit function reports directly to the statutory governing body, where applicable through the risk committee or the audit committee, and keeps senior management or, where applicable, the management committee informed of its findings. For more information on the NBB's prudential expectations regarding the internal audit function, please see the Regulation of 19 May 2015 and Circular NBB_2015_21 as well as paragraphs 191 to 201 of EBA/GL/2021/14.

4.5. ICT SECURITY AND BUSINESS CONTINUITY MANAGEMENT

4.5.1. ICT SECURITY

Statutory and regulatory framework

1. Brokerage Supervision Act: Article 17 §1(7)
2. NBB circulars:
   - Circular NBB_2021_21 of 26 October 2021 on the EBA Guidelines on major incident reporting
   - Circular NBB_2020_23 of 16 June 2020 on the EBA Guidelines on ICT and security risk management
   - Circular NBB_2019_09 of 8 May 2019 on reporting under the EBA Guidelines on security measures for operational and security risks under PSD2
   - Circular NBB_2019_19 of 19 July 2019 on outsourcing
   - Circular NBB_2015_32 of 18 December 2015 on the NBB's additional prudential expectations regarding operational business continuity and security of systemically important financial institutions
   - Communication NBB_2011_05 of 27 October 2011 on the NBB's prudential expectations on sound management of operational risk
   - Circular NBB_2009_17 of 7 April 2009 on prudential requirements for the online provision of financial services
   - Circular PPB 2005/2 of 10 March 2005 on sound management practices aimed at ensuring the continuity of financial institutions
3. International reference documents: //

4:175 Article 17 §1(7) of the Brokerage Supervision Act stipulates that IT control and security mechanisms should be put in place which are appropriate to the firm's activities and sufficiently robust to guarantee the security and authentication of the means of transferring information, minimise the risk of data corruption and unauthorised access, and prevent information leaks in order to maintain data confidentiality at all times.

4:176 For example, the statutory governing body should ensure that the firm's governance system, in particular the risk management and internal control system, adequately manages risks related to information and communication technology (ICT) and information security.

4:177 Firms should, as part of their governance system and in accordance with the principle of proportionality, establish an information security function whose tasks include: (i) providing guidance on the firm's information security vision and strategy, taking into account all relevant information; (ii) ensuring that the information security objectives and measures defined in this strategy are translated into a comprehensive information security policy framework; (iii) properly communicating this information security policy framework to all stakeholders, both internally and, as appropriate, externally; (iv) assessing, monitoring and ensuring compliance with the information security strategic framework and, as appropriate, adapting it; and (v) establishing security risk management and reporting processes that are integrated into the firm's overall risk management framework.

4:178 It is recommended that the information security function be a senior position (N-1 level) within the firm who can report directly to the statutory governing body and senior management or, where applicable, the management committee. Responsibility for the information security function may be assigned to the chief information security officer (CISO).

4:179 For more information, please see the relevant NBB circulars (in particular Circular NBB_2019_19 which applies to all outsourcing, including cloud outsourcing, and Circular NBB_2009_17 on online services, etc.).

4.5.2. BUSINESS CONTINUITY MANAGEMENT

Statutory and regulatory framework

1. Brokerage Supervision Act: Article 17 §1(9)
2. NBB circulars:
   - Circular NBB_2017_29 of 30 November 2017 on crisis management
   - Circular PPB 2005/2 of 10 March 2005 on sound management practices aimed at ensuring the business continuity of financial institutions
3. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 202 to 207

4:180 Firms should establish a sound business continuity management and recovery plan to ensure their ability to operate on a going concern basis and to limit losses in the event of severe business disruption.

4:181 For more information on business continuity management, please see paragraphs 202 to 207 of EBA/GL/2021/14.

4:182 In addition, Circular PPB 2005/2 sets out a number of criteria - translated into sound management practices - for assessment by the NBB of business continuity plans.

5. GOVERNANCE AT GROUP LEVEL

Statutory and regulatory framework

1. Brokerage Supervision Act: Articles 159 to 199
2. NBB circulars: /
3. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 77 to 84

5:1 Good governance requirements also apply in the context of a group, as defined in Article 25 of Directive (EU) 2019/2034. Indeed, rules of good governance should be complied with on a consolidated and, if applicable, sub-consolidated basis. This chapter applies to all types of groups (at EEA level, Member State level and Belgian level) and subgroups (at Member State or Belgian level).

5:2 With regard to group supervision, a distinction is made between:
- investment firms that are part of a group consisting of a parent company and its subsidiaries, including at least one credit institution (a "banking group"); and
- investment firms that are part of a group consisting of a parent company and its subsidiaries, not including a credit institution (an "investment firms group").

5:3 In the first case, consolidated supervision is governed by the Banking Act[50] and Regulation (No) 575/2013, and reference should be made to the Governance Manual for the Banking Sector which details the governance rules applicable to groups, distinguishing between groups for which a Belgian entity is responsible for ensuring compliance with the prudential rules on a consolidated basis and those for which an institution governed by the law of another Member State or a third country is responsible for doing so.

5:4 For the second group, the European legislature established a new regime in Regulation (No) 2019/2033 and Directive 2019/2034, which has been transposed into Belgian law by the Brokerage Supervision Act. This legislation concerns both the consolidated supervision of investment firms groups and supervision of compliance with the capital test for groups of investment firms with a simpler structure and risk profile. Under this special regime, the parent company of the group can, in lieu of prudential consolidation, maintain sufficient capital to cover the book value of the holdings in its subsidiaries.

5:5 The following sections focus on the second group only, covered by Section III of Chapter IV of the Brokerage Supervision Act. Section IV concerns the supplementary supervision of conglomerates of stockbroking firms, regardless of whether a credit institution forms part of the group to which they belong. As this supervision is governed at European level by Directive 2011/89/EU, Section IV refers to the transposition of this directive by means of the Banking Act.

5.1. Governance rules applicable to groups of investment firms for which a Belgian entity is responsible for ensuring compliance with the prudential rules on a consolidated basis by the group and its entities

5:6 This section concerns:
1) groups for which the ultimate parent company in Belgium or another EEA country is a Belgian stockbroking firm; and
2) groups for which the ultimate parent company in Belgium or another EEA country is a Belgian investment holding company or a Belgian (mixed) financial holding company.

The firm at the head of such a group is referred to as the "Belgian institution responsible for the group".

[50] Act of 25 April 2014 on the legal status and supervision of credit institutions, transposing Directive 2013/36/EU.

5:7 Pursuant to Article 163 of the Brokerage Supervision Act, the Belgian institution responsible for the group must comply (on a consolidated and/or, where applicable, sub-consolidated basis) with Articles 17, 23 to 40, 56 to 59, 66 to 78, 86 and 109 of the Brokerage Supervision Act and (i) ensure that the governance arrangements, processes and mechanisms are consistent and well integrated on a consolidated or sub-consolidated basis, (ii) assess the influence of the companies within the scope of consolidation on each other, and (iii) obtain all data and information relevant for supervision of the group or subgroup.

5:8 All rules relating to good governance se out in this manual apply *mutatis mutandis* at group level.

5:9 In practice, the Belgian institution responsible for the group should implement arrangements, processes and mechanisms to ensure sound and consistent governance for the group or subgroup on a consolidated basis. Please see paragraph 5:9 of the Governance Manual for the Banking Sector, which applies by analogy.

5:10 For more information, please see paragraphs 77 to 84 of EBA/GL/2021/14.

5.2. Governance rules applicable to Belgian stockbroking firms and Belgian investment holding companies within a group for which an institution governed by the law of another Member State is responsible

5:11 For Belgian stockbroking firms and Belgian investment holding companies belonging to a group for which an institution governed by the law of another Member State is responsible, it should be ensured that the organisation and management of the group do not detract from the responsibilities of the statutory governing body and senior management or, where applicable, the management committee of the Belgian firm as regards the conduct of the firm concerned.

5.2.1. General rule

5:12 The starting point for the prudential assessment of group governance is that the firm governed by the law of another Member State that is responsible for the group and its subsidiaries, including the Belgian subsidiary(ies), should be in agreement and operate in a transparent and balanced manner, focusing on optimal management of the activities of the different supervised institutions and adequate monitoring of the risks faced by the individual institutions and the group as a whole.

5:13 In this respect, the institution responsible for the group, as the entity that defines the group's overall policy and strategy, should ensure that the group is managed in the best possible manner, with respect for the legal personality of the various subsidiaries and without prejudice to any measures the institution responsible for the group may take to control the reputational risk that could arise from inappropriate behaviour by a subsidiary. In accordance with paragraph 77 of EBA/GL/2021/14, the firm governed by the law of another Member State that is responsible for the group should consider the interests of all subsidiaries and how strategies and policies contribute to the interest of each one and of the group as a whole over the long term.

5.2.2. Distribution of tasks between the firm governed by the law of another Member State that is responsible for the group, on the one hand, and the Belgian subsidiary, on the other hand

5:14 It is the responsibility of the subsidiary not to undermine the necessary coherence within the group and to ensure that information can flow sufficiently upstream and downstream within the consolidated group.

5:15 Without prejudice to the role played by the institution responsible for the group, the Belgian subsidiary's governing bodies should also ensure that the management of the group complies with the rules and obligations to which they are subject as an entity with separate legal personality and as a regulated institution. The Belgian subsidiary's statutory governing body and senior management or, where applicable, the management committee should ensure in particular that the organisation of the group complies with the rules and obligations to which the subsidiary is subject in its capacity as an entity with separate legal personality and as a regulated institution.

5.2.3. Management of intra-group conflicts of interest

5:16 Conflicting interests at group level should be identified and prevented or managed. These may include:
  i. conflicts of interest arising from the performance of mutually conflicting activities;

ii. intra-group transactions and the allocation of capital within the group;
iii. diverging interests between the institution responsible for the group and subsidiaries or between subsidiaries, e.g. regarding the allocation of corporate and regulatory opportunities;
iv. decisions of the group which, for the various activities carried out by different subsidiaries, impact differently the management of their financial situation.

5:17 In the exercise of their corporate responsibility, the directors of the subsidiary should dispose of appropriate resources to safeguard the firm's corporate interest while keeping in mind its stakeholders. For this purpose, intra-group mechanisms should be put in place to identify certain decisions or practices at group level that could give rise to an intra-group conflict of interest and bring them to the attention of the governing bodies of the subsidiary and the institution responsible for the group. In the case of intra-group operations or transactions that could be material for the subsidiary, an *ad hoc* committee of independent directors should be set up to issue an opinion, for consideration by the subsidiary's statutory governing body, on the subsidiary's interest in the context of such intra-group operations or transactions.

5:18 Depending on the group's governance model, these internal mechanisms should also be based, for example, on a robust supervisory function within the subsidiary's statutory governing body, directors on the subsidiary's statutory governing body who are independent from the institution responsible for the group or subgroup, or effective independent control functions within the subsidiary.

5.3. Governance rules applicable to Belgian stockbroking firms and investment holding companies belonging to third-country groups

5:19 The governance rules set out in section 5.2 above apply *mutatis mutandis* to third-country groups.

5:20 In accordance with Articles 189 and 190 of the Brokerage Supervision Act, third-country groups whose activities through subsidiaries in the EU exceed the threshold of €40 billion are required to establish an intermediate parent company in the European Union. This requirement is intended to allow for more comprehensive supervision of activities in the EU and facilitate resolution. Where such an intermediate parent company is established in the European Union, the rules applicable to EU banking groups apply.

6. PRUDENTIAL REPORTING ON GOVERNANCE AND TRANSPARENCY

6.1. GOVERNANCE REPORTING

6:1 The two main[51] prudential reporting requirements in terms of governance are (i) the governance memorandum and (ii) senior management's report on assessment of the internal control system.

6.1.1. GOVERNANCE MEMORANDUM

Statutory and regulatory framework

1. Brokerage Supervision Act: Article 17 §..., 19 and 56 §6
2. NBB circulars:
   - See Annex 2 to this manual transposing Annex I to EBA/GL/2021/14
3. International reference documents:
   - EBA/GL/2021/14 on internal governance => Annex I

6.1.1.1. Governance memorandum

6:2 Each firm should describe and document its internal governance structure in a governance memorandum. The statutory governing body should approve the governance memorandum and ensure that it is kept up to date.[52]

6:3 The governance memorandum is a prudential document which forms an integral part of the licence application file and is, as such, confidential.

6:4 The memorandum is primarily the responsibility of the firm. It should be updated whenever significant changes occur that affect the firm's governance structure and organisation and should be assessed at least once a year by the statutory governing body, in accordance with Articles 19 and 56 of the Brokerage Supervision Act. The firm should provide a detailed explanation if it does not comply with best practices provided for in this manual or in circulars or international guidelines (the "comply or explain" approach).

6:5 An outline for the governance memorandum is annexed to this manual. The use of this outline is optional. It is also good practice to append to the governance memorandum a list of governance policies and internal by-laws in force, if possible along with the relevant documents or links thereto.

6.1.1.2. Group governance memorandum

6:6 Where the firm is part of a group that falls under the supervision of the NBB, the governance memorandum drawn up for the firm may form part of the group memorandum.[53] Where it is integrated into a group memorandum, the statutory governing body of each firm subject to supervision to which the memorandum applies should approve it.

6:7 In addition to any relevant aspects relating to the subsidiaries that form part of the group, the group memorandum should cover the situation of the institution responsible for the group and of the group as such, in particular:

[51] Without prejudice to other prudential reporting requirements provided for by NBB circulars and communications on qualitative reporting (the compliance report, AML report, reporting on loans to managers, assessment of the compliance function, etc.).

[52] Articles 21 §3, 23 and 56 §6 of the Brokerage Supervision Act.

[53] Article 21 §3, second subparagraph, of the Brokerage Supervision Act.

i. a description of the objectives and interests of the group versus the areas of activity and interests of the subsidiaries;

ii. a description of the steering of the group and the organisation of group supervision of the subsidiaries;

iii. the concrete distribution of tasks between the institution responsible for the group and the subsidiaries, including a description of the subsidiaries' own responsibilities;

iv. an organisational chart including all corporate bodies and/or persons bearing responsibility for administration and strategy, operational management of the group and its entities, the business lines and centralised services as well as all relevant functions for prudential purposes within the institution responsible for the group and the subsidiaries (internal audit, compliance, risk management, actuary, accounting, etc.);

v. the policy and rules taken into consideration by the group as regards intra-group outsourcing, management of conflicting interests, etc.

6.1.1.3. Verification by the NBB

6:8 The memorandum and any significant changes thereto should be transmitted to the NBB.

6.1.2. ASSESSMENT REPORT ON THE INTERNAL CONTROL SYSTEM

Statutory and regulatory framework

1. Brokerage Supervision Act: Article 59 §2
2. NBB circulars:
   - Uniform letter of 16 November 2015 to institutions on senior management's assessment report on the internal control system
   - Circular NBB_2011_09 of 20 December 2011 on senior management's assessment report on the internal control system

6:9 Article 59 §2 of the Brokerage Supervision Act provides that the stockbroking firm's senior management or, where applicable, its management committee should report to the statutory governing body, the certified auditor and the NBB on its assessment of the effectiveness of the organisational structure referred to in Article 17 of the Brokerage Supervision Act, including specific organisational measures for the provision of investment services and the measures taken, if any, to remedy any deficiencies that may have been identified.

6:10 Such a report should be prepared at least every two years. However, although this report is now biannual, the firm should nevertheless provide the following information in the year in which reporting is not required:

- a summary of the main developments and changes made or, in the absence thereof, the significant developments and changes introduced by senior management during the reporting period in the context of internal control (including for investment services and activities); and
- a statement by senior management formally confirming that the organisation and measures taken (including with regard to investment services and activities) comply with statutory and regulatory requirements.

6:11 Circular NBB_2011_09 provides further information on the various reports that the firm's senior management should submit to the certified auditor and the NBB. This circular also sets out the NBB's expectations with regard to periodic prudential reporting. For more information, please refer to this circular.

6.2. TRANSPARENCY TOWARDS STAFF AND THE PUBLIC

Statutory and regulatory framework

1. Brokerage Supervision Act: Article 86
2. Delegated Regulation 575/2013 (Articles 435 and 450) and Regulation (EU) 2019/2033 (Articles 46 to 53)
3. NBB circulars: /
4. International reference documents:
   - EBA/GL/2021/14 on internal governance => paragraphs 208 to 211

6:12 The firm's strategies, policies and procedures should be communicated to all relevant staff throughout the firm. For more information, please see paragraphs 208 and 201 of EBA/GL/2021/14.

6:13 As regards transparency towards the public, Article 86 of the Brokerage Supervision Act requires firms to publish on their website the relevant information from their governance memorandum, including at least the items referred to in paragraph 211 of EBA/GL/2021/14.

6:14 Disclosure of the risk management objectives and policies is governed directly by Article 48 *et seq.* of Regulation (No) 2019/2033. The firm should publish minimum information concerning its governance, risk management policy, equity, remuneration policy, investment policy, environmental, social and governance risks, etc. Please see Regulation (No) 2019/2033 for more information on this subject.

ANNEX 1: GOVERNANCE MEMORANDUM OUTLINE

1. Shareholder structure
2. Group structure if applicable (legal and functional structure, organisational chart)
3. Policy as regards the composition and functioning of the management bodies (possibly with a description of the group's impact, if applicable)
   (a) number, length of term of office, rotation, age, follow-up, etc.
   (b) selection criteria (including diversity considerations)
   (c) nomination procedure (new term of office/renewal) and resignation/non-renewal
   (d) independent directors
   (e) remuneration policy
      i. executive members of the statutory governing body
      ii. non-executive members of the statutory governing body
4. Governance structure and organisational chart (possibly with a description of the group's impact, if applicable)
   (a) statutory governing body (in this case, the board of directors)
      i. composition (including meeting of the quantitative diversity target)
      ii. functioning (by-laws)
      iii. internal allocation of tasks, if applicable
      iv. specialised committees
         - composition
         - functioning
   (b) senior management or, where applicable, management committee
      i. composition (including meeting of the quantitative diversity target)
      ii. functioning (by-laws)
      iii. internal allocation of tasks between members
   (c) other committees
5. Internal control and key functions (possibly with a description of the group's impact, if applicable)
   (a) internal control framework (description of each function, including its organisation, resources and authority)
   (b) support functions (secretary general, legal affairs, human resources, communication)
   (c) Independent control functions
      i. internal audit
      ii. compliance
      iii. risk management
   (d) risk strategy and risk management framework
   (e) measures to prevent money laundering and counter the financing of terrorism
6. Organisational structure (possibly with a description of the group's impact, if applicable)
   (a) operational structure, business lines, matrix management and allocation of competencies and responsibilities
   (b) outsourcing
   (c) range of products and services and new product approval policy
   (d) geographical scope of activity
      i. freedom to provide services
      ii. branches
      iii. subsidiaries, joint ventures, etc.
   (e) use of offshore centres
7. Remuneration policy
   (a) governance
   (b) global policy for all staff members
   (c) identified staff
      i. selection process
      ii. specific rules (risk alignment, deferral, instruments, etc.)
   (d) gender pay gap

8. Code of conduct and behaviour (possibly with a description of the group's impact, if applicable)
   (a) strategic objectives and corporate values
   (b) codes and internal rules, prevention policy, etc.
   (c) conflict of interest policy (at firm level and for staff)
   (d) whistleblowing procedure
   (e) handling of customer complaints
9. ICT security and business continuity
   (a) ICT security function
   (b) ICT security mechanism
   (c) business continuity policy
10. Policy on disclosure of the applied principles
11. Status and date of the corporate governance memorandum
   (a) preparation
   (b) last amendment
   (c) last review
   (d) approval by the statutory governing body

ANNEX 2: EBA GUIDELINES ON INTERNAL GOVERNANCE FOR INVESTMENT FIRMS (EBA/GL/2021/14)

EBA/GL/2021/14

22 November 2021

Final report on

Guidelines on internal governance under Directive (EU) 2019/2034

EBA EUROPEAN BANKING AUTHORITY

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Executive summary

For several years now, internal governance issues have received increased attention from various international bodies. Their main aim has been to correct financial institutions' weak or superficial internal governance practices, including compliance with the framework to prevent money laundering and terrorist financing, as the reinforcement of internal governance arrangements is a critical issue for the sustainable growth of market-based financing.

Sound internal governance arrangements are fundamental if investment firms are to operate well as part of the financial system. Directive (EU) 2019/2034 sets out governance requirements for investment firms and, in particular, stresses the responsibility of the management body to ensure sound governance arrangements, the importance of a strong supervisory function that challenges management's decision-making and the need to establish and implement a sound risk strategy, risk appetite, risk culture and risk management framework.

To further harmonise investment firms' internal governance arrangements, processes and mechanisms within the EU, in line with the requirements introduced by Directive (EU) 2019/2034, the European Banking Authority (EBA) is mandated by Article 26(4) of Directive (EU) 2019/2034 to develop guidelines in this area. The guidelines apply to investment firms as defined in Article 4(1)(1) of Directive (EU) 2014/65 that do not meet all of the conditions for qualifying as small and non-interconnected investment firms under Article 12(1) of Regulation (EU) 2019/2033. These requirements apply regardless of the investment firms' governance structures (unitary board, dual board or other structure). However, the guidelines do not advocate or prefer any specific structure. The terms 'management body in its management function' and 'management body in its supervisory function' should be interpreted in accordance with the applicable law within each Member State.

The guidelines complete the various governance provisions in Directive (EU) 2019/2034, taking into account the principle of proportionality, by specifying the tasks, responsibilities and functioning of the management body, and the organisation of investment firms, including the need to create transparent structures that allow for the supervision of all their activities. The guidelines also specify in more detail the requirements under Directive (EU) 2019/2034 and aim to ensure the sound management of all risks. Risks need to be managed across all three lines of defence. While the business needs to manage its risks, the guidelines stress the responsibilities of the second line of defence (the independent risk management and compliance function) and also the third line of defence (the internal audit function).

The guidelines are consistent with the guidelines on internal governance for credit institutions and with international standards and, in particular, set out provisions that aim to foster a sound risk culture to be implemented by the management body, strengthening the management body's oversight of the investment firm's activities and implementing a sound risk management framework.

Background and rationale

1. Trust in the reliability of the financial system is crucial for its proper functioning and a prerequisite if it is to contribute to the economy as a whole. Consequently, effective internal governance arrangements are fundamental to the sustainable growth of market-based funding.

2. In recent years, internal governance issues have received increased attention from various international bodies[1]. Their main aim has been to correct financial institutions' weak or superficial internal governance practices, as identified during the financial crisis and during ongoing supervision by competent authorities. In addition, there has recently been a greater focus on conduct-related shortcomings and activities in offshore financial centres, and in the area of money laundering and terrorist financing.

3. In some cases, the absence of effective checks and balances within financial institutions resulted in a lack of effective oversight of management decision-making, which led to short-term and excessively risky management strategies. Weak oversight by the management body in its supervisory function has been identified as a contributing factor. The management body, both in its management function and, in particular, in its supervisory function, might not have understood the complexity of the business and the risks involved. Consequently, these bodies failed to identify and constrain excessive risk-taking in an effective manner.

4. Internal governance frameworks, including internal control mechanisms and risk management, were often not sufficiently integrated within financial institutions or groups. These functions were not regarded as a high priority, which impacted the stability of markets as a result. In many investment firms there was a lack of a uniform risk methodology and terminology, which meant that there was no holistic view of all risks. Internal control functions often lacked appropriate resources, status and/or expertise.

5. Conversely, sound internal governance practices helped some financial institutions to manage the financial crisis significantly better than others. These practices included the setting of an appropriate risk strategy and appropriate risk appetite levels, a holistic risk management framework and effective reporting lines to the management body.

6. Against this backdrop, there is a clear need to address the potentially detrimental effects of poorly designed internal governance arrangements on the sound management of risk, to ensure effective oversight by the management body, in particular in its supervisory function, to promote a sound risk culture at all levels of investment firms and to enable competent authorities to supervise and monitor the adequacy of internal governance arrangements.

[1] IOSCO/OECD

Legal basis

7. To further harmonise investment firms' internal governance arrangements, processes and mechanisms within the EU, the EBA, in cooperation with the ESMA, is mandated under Article 26(4) of Directive (EU) 2019/2034 to develop guidelines in this area.

8. Article 26 (1) of Directive (EU) 2019/2034 requires investment firms to have robust governance arrangements, including a clear organisational structure with well-defined, transparent and consistent lines of responsibility.

9. Article 28 of Directive (EU) 2019/2034 sets out requirements for the involvement of the management body in risk management and the setting up of a risk committee for investment firms.

10. In accordance with Article 25 of Directive (EU) 2019/2034 and Article 7 of Regulation (EU) 2019/2033, these guidelines apply on an individual and consolidated basis. For this purpose, parent undertakings and subsidiaries subject to Directive (EU) 2019/2034 must ensure that internal governance arrangements, processes and mechanisms in their subsidiaries are consistent and well integrated and that the governance arrangements on a consolidated basis are robust. In particular, it should be ensured that parent undertakings and subsidiaries subject to this Directive implement such arrangements, processes and mechanisms in their subsidiaries that are not subject to this Directive, including those established in third countries – including offshore financial centres.

11. The guidelines should be read, taking into account and without prejudice to Articles 9, 16, 23 and 24 of Directive (EU) 2014/65, the Commission Delegated Regulation (EU) 2017/5652 and the Commission Delegated Directive (EU) No 2017/593[3], in conjunction with the EBA guidelines on sound remuneration policies for investment firms, the joint EBA and ESMA guidelines on the assessment of the suitability of members of the management body and key function holders, the EBA guidelines on the supervisory review and evaluation process (SREP), the ESMA guidelines on certain aspects of the MiFID II compliance function requirements, the ESMA guidelines on product governance and the Regulatory Technical Standards on disclosures.

Rationale and objective of the guidelines

12. Internal governance includes all standards and principles concerned with setting an investment firm's objectives, strategies and risk management framework; how its business is organised; how responsibilities and authority are defined and clearly allocated; how reporting

[2] Commission Delegated Regulation (EU) 2017/65 supplementing Directive (EU) 2014/65 of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive

[3] Commission Delegated Directive (EU) 2017/593 of 7 April 2016 supplementing Directive (EU) 2014/65 of the European Parliament and of the Council with regard to safeguarding of financial instruments and funds belonging to clients, product governance obligations and the rules applicable to the provision or reception of fees, commissions or any monetary or non-monetary benefits

lines are set up and what information they convey; and how the internal control framework is organised and implemented, including accounting procedures and remuneration policies. Internal governance also encompasses sound information technology systems, outsourcing arrangements and business continuity management.

13. Combating money laundering and terrorist financing is essential for maintaining the stability and integrity of the financial system. Uncovering the involvement of an investment firm in money laundering and terrorist financing might have an impact on its viability and on trust in the financial system. Together with the authorities and bodies (e.g. AML supervisors and financial intelligence units) responsible for ensuring compliance with anti-money laundering rules under Directive (EU) 2015/849, competent authorities have an important role to play in identifying and tackling weaknesses in this area. In this context, the guidelines clarify that identifying, managing and mitigating money laundering and financing of terrorism risks is part of sound internal governance arrangements and investment firms' risk management framework.

14. In the same way, investment firms should take into account environmental, social and governance (ESG) risk factors within their risk management framework.

15. The guidelines are intended to apply to all existing board structures without interfering with the general allocation of competences in accordance with national company law or advocating any particular structure. Accordingly, they should be applied irrespective of the board structure used (unitary or dual board structure or another structure) and across Member States. The management body, as defined in points (23) and (24) of Article 3(1) of Directive (EU) 2019/2034, should be understood as having management (executive) and supervisory (non-executive) functions.

16. The terms 'management body in its management function' and 'management body in its supervisory function' are used throughout these guidelines without referring to any specific governance structure, and references to the management (executive) or supervisory (non-executive) function should be understood as applying to the bodies or members of the management body responsible for that function in accordance with national law.

17. In Member States where the management body delegates, partially or fully, the executive function to a person or an internal executive body (e.g. a chief executive officer (CEO), management team or executive committee), the persons who perform these executive functions and direct the business of the institution on the basis of that delegation should be understood as constituting the management function of the management body. For the purposes of these guidelines, any reference to the management body in its management function should be understood as also including the members of the executive body or the CEO, as defined in these guidelines, even if they have not been proposed or appointed as formal members of an investment firm's governing body or bodies under national law.

18. The management body is empowered to set the investment firm's strategy, objectives and overall direction, and oversees and monitors management decision-making. In its management function, the management body directs the investment firm. Senior management is accountable to the management body for the day-to-day running of the investment firm. In its supervisory function, the management body oversees and challenges the management function and provides appropriate advice. The oversight roles include reviewing the performance of the management function and the achievement of objectives, challenging the strategy, and monitoring and scrutinising the systems that ensure the integrity of financial information as well as the soundness and effectiveness of risk management and internal controls.

19. Taking into consideration all the existing governance structures provided for by national laws, competent authorities should ensure the effective and consistent application of the guidelines in their jurisdictions in accordance with the rationale and objectives of the guidelines themselves. For this purpose, competent authorities may clarify the governing bodies and functions to which the tasks and responsibilities set forth in the guidelines pertain, where this is appropriate to ensure the proper application of the guidelines in accordance with the governance structures provided for under national company law.

20. Having independent directors within the supervisory function of the management body helps to ensure that the interests of all internal and external stakeholders are considered and that independent judgement is exercised where there is an actual or potential conflict of interest[4].

21. With regard to the composition of committees and in particular with regard to independent members, the guidelines take into account the principle of proportionality. Simpler provisions have therefore been introduced for smaller investment firms.

22. While not subject to the governance requirements in accordance with Article 25 of Directive (EU) 2019/2034, small and non‑interconnected investment firms should have robust strategies, policies, processes and systems in place for the identification, measurement, management and monitoring of material sources and effects of risk to clients and any material impact on own funds, material sources and effects of risk to market and any material impact on own funds and liquidity risk over an appropriate set of time horizons, including intra‑day, so as to ensure that the investment firm maintains adequate levels of liquid resources in accordance with Article 29(3) of Directive (EU) 2019/2034.

23. The guidelines are consistent with the 'three lines of defence' model in identifying the functions within investment firms responsible for addressing and managing risks. Investment firms should establish and maintain a permanent and effective compliance function that operates independently from the business it controls and, where appropriate and taking into account the application of the proportionality principle, establish and maintain risk management and internal audit functions that operate independently. Where those functions

[4] In this regard, the guidelines are based on the Commission Recommendation of 15 February 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board.

are not established, investment firms should ensure that the policies and procedures that they have adopted and implemented regarding risk management and internal audit achieve the same objectives.

24. The business lines, as part of the first line of defence, take risks and are directly and permanently responsible for their operational management. For that purpose, business lines should have appropriate processes and controls in place that aim to ensure risks are identified, analysed, measured, monitored, managed, reported and kept within the limits of the investment firms' risk appetite, and that the business activities are in compliance with external and internal requirements.

25. Not only business lines, but also other functions or units, e.g. HR, legal or information technology, are responsible for managing their risks and having appropriate controls in place. Other functions or units are mainly exposed to operational and reputational risks that must be considered by the compliance function and risk management function when forming an enterprise-wide holistic view of all risks. All other functions or units should also be subject to monitoring and oversight by the independent risk management function, where established, and by the compliance function as part of a risk-based approach.

26. The independent risk management function, where established, and the compliance function form the second line of defence. The risk management function facilitates the implementation of a sound risk management framework throughout the investment firm and is responsible for further identifying, monitoring, analysing, measuring, managing and reporting risks and forming a holistic view of all risks on an individual and, where applicable, consolidated basis. It challenges and assists in the implementation of risk management measures by the business lines in order to ensure that the processes and controls in place in the first line of defence are properly designed and effective. The compliance function monitors compliance with legal requirements and internal policies, provides advice on compliance issues to the management body and other relevant staff, and establishes policies and processes to manage compliance risks and to ensure compliance[5]. The compliance function and, where established, the risk management function intervene as necessary to ensure the modification of internal control and risk management systems within the first line of defence.

27. The internal audit function, where established as an independent third line of defence, conducts risk-based and general audits and reviews the internal governance arrangements, processes and mechanisms to ascertain that they are sound and effective, implemented and consistently applied. The internal audit function is also in charge of the independent review of the first two lines of defence including other internal functions, units and business lines. Investment firms that do not establish an independent audit function must establish other appropriate audit policies and procedures. In any case, the ultimate responsibility for audits remains with the management body.

28. To ensure their proper functioning, all internal control functions need to perform their tasks independently, have the appropriate financial and human resources and report directly to the

[5] See also ESMA Guidelines on certain aspects of the MiFID II compliance function requirements

management body. Within all three lines of defence, appropriate internal control procedures, mechanisms and processes should be designed, developed, maintained and evaluated under the ultimate responsibility of the management body.

29. The requirements on governance arrangements under the IFD are very similar to the requirements under the CRD and apply to investment firms, unless they meet all of the conditions to qualify as small and non-interconnected investment firms under Article 12(1) of Regulation (EU) 2019/2033 (IFR) or are subject to the CRD requirements in accordance with Article 2(2) IFD.

30. The CRD and IFD are both based on the same governance concepts and principles of good governance arrangements, while taking into account that investment firms are often smaller or less complex. Therefore a more proportionate approach is taken for such investment firms, in particular regarding the establishment of committees and control functions. Most investment firms that are now subject to the governance provisions under the IFD have been subject to the requirements under the CRD, and consistency should therefore be ensured to the extent possible to reduce the implementation costs for such firms and to ensure that consistent group-wide policies can be applied.

31. The guidelines and the principle of proportionality cannot change the minimum requirements included in the IFD. The same holds true with regard to the requirements under MiFID that apply to all investment firms. All provisions within the guidelines are subject to the principle of proportionality, meaning that they are to be applied in a manner that is appropriate, taking into account in particular the investment firm's size, internal organisation and nature, and the complexity of its activities. However, the principle of proportionality does not mean that investment firms are permitted to not meet certain requirements, i.e. requirements cannot be waived unless the IFD explicitly allows for such waivers when the underlying conditions are met.

32. The guidelines also specify the requirements under Article 26 of Directive (EU) 2019/2034, in particular with regard to the setting up of new structures e.g. in third countries, including also in offshore financial centres. These requirements aim to increase the transparency of and reduce the risks connected with such activities. Guidelines are also provided regarding investment firms' reporting on governance arrangements, including in relation to such structures.

33. The guidelines aim to establish a sound risk culture in investment firms. Risks should be taken within a well-defined framework in line with the investment firms' risk strategy and risk appetite. This includes the establishment of and ensuring compliance with a system of limits and controls. Risks within new products[6] and business areas, but also risks that may result from changes to investment firms' products, processes and systems, are to be duly identified, assessed, appropriately managed and monitored. The risk management function and compliance function should be involved in the establishment of the applicable framework and

[6] See also ESMA Guidelines on MiFID II products governance

the approval of such changes to ensure that all material risks are taken into account and that the investment firms comply with all internal and external requirements.

34. To ensure objective decision-making, oversight and compliance with external and internal requirements, including investment firms' strategies and risk limits, investment firms should implement a conflict of interest policy and internal whistleblowing procedures.

35. In order to manage conflicts of interest, the management body should ensure that a framework for the identification and, where necessary, mitigation of conflicts of interest is in place. The investment firm, its organisational substructures, staff and shareholders hold different interests that should be considered in such a framework in order to ensure that decisions are taken objectively without the undue influence of conflicts of interest. Examples of typical sources of conflicts of interest are diverging economic interests of different parties involved, or close links between decision-makers and contractual parties.

36. The management body has the highest decision-making powers. Consequently, the identification and management of conflicts of interest of members of the management body and parties closely related to the members of the management body is a cornerstone of sound internal governance practices. Therefore, the guidelines also specify the measures that should be implemented by investment firms to prudently manage conflicts of interests that may arise from entering into transactions, including with members of the management body and their related parties. Those transactions may include loans where there is the possibility for investment firms to grant loans as ancillary services.

EBA/GL/2021/14

22 November 2021

Guidelines

on internal governance under Directive (EU) 2019/2034

1. Compliance and reporting obligations

Status of these guidelines

1. These guidelines are issued pursuant to Article 16 of Regulation (EU) No 1093/2010[7]. In accordance with Article 16(3) of Regulation (EU) No 1093/2010, competent authorities and financial institutions, including investment firms, must make every effort to comply with the guidelines.

2. The guidelines set out the EBA view of appropriate supervisory practices within the European System of Financial Supervision or of how Union law should be applied in a particular area. Competent authorities as defined in Article 4(2) of Regulation (EU) No 1093/2010 to whom the guidelines apply should comply by incorporating them into their practices as appropriate (e.g. by amending their legal framework or their supervisory processes), including where guidelines are directed primarily at investment firms.

Reporting requirements

3. In accordance with Article 16(3) of Regulation (EU) No 1093/2010, a competent authority must notify the EBA as to whether it complies or intends to comply with these guidelines, or otherwise stating the reasons for non-compliance, by ([dd.mm.yyyy]). In the absence of any notification by this deadline, the competent authority will be considered by the EBA to be non-compliant. Notifications should be sent by submitting the form available on the EBA website to compliance@eba.europa.eu with the reference 'EBA/GL/2021/14'. Notifications should be submitted by persons with appropriate authority to report compliance on behalf of their competent authority. Any change in the status of compliance must also be reported to the EBA.

4. Notifications will be published on the EBA website, in line with Article 16(3) of Regulation (EU) No 1093/2010.

[7] Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (OJ L 331, 15.12.2010, p. 12)

2. Subject matter, scope and definitions

Subject matter

5. These guidelines specify, in accordance with Article 26(4) of Directive (EU) 2019/2034[8], the internal governance arrangements, processes and mechanisms that investment firms should implement in accordance with Title IV, Chapter 2, Section 2 of that Directive to ensure their effective and prudent management.

6. The guidelines apply without prejudice to the provisions set out in in Articles 9, 16, 23 and 24 of Directive (EU) 2014/65, in the Commission Delegated Regulation (EU) 2017/565 and in the Commission Delegated Directive (EU) 2017/593.

Addressees

7. These guidelines are addressed to competent authorities as referred to in Article 4(2), point (viii) of Regulation (EU) 1093/2010 and defined in Article 3(1), point 5 of Directive (EU) 2019/2034, and to financial institutions as referred to in Article 4(1) of Regulation (EU) 1093/2010 that are investment firms as defined in Article 4(1)(1) of Directive (EU) 2014/65, that do not fall under Article 2(2) of Directive (EU) 2019/2034 and do not meet all of the conditions to qualify as small and non-interconnected investment firms under Article 12(1) of Regulation (EU) 2019/2033.

Scope of application

8. These guidelines apply in relation to investment firms' governance arrangements as required under Directive (EU) 2019/2034, including their organisational structure and the corresponding lines of responsibility, and also to the processes to identify, manage, monitor and report all risks[9] that they are or might be exposed to, and to the internal control framework.

9. These guidelines apply on an individual and consolidated basis within the scope of application set out in accordance with Article 25 of Directive (EU) 2019/2034.

10. The guidelines intend to embrace all existing board structures and do not advocate any particular structure. The guidelines do not interfere with the general allocation of competences in accordance with national company law. Accordingly, they should be applied

[8] Directive (EU) 2019/2034 of the European Parliament and of the Council of 27 November 2019 on the prudential supervision of investment firms and amending Directives 2002/87/EC, 2009/65/EC, 2011/61/EU, 2013/36/EU, 2014/59/EU and 2014/65/EU

[9] Any reference to risks in these guidelines should include all risks to which investment firms are or may be exposed, including risks to clients, risks to the market, risks to the investment firm and liquidity risks, operational risks including legal and IT risks and reputational risks, ESG risks and money laundering and terrorist financing risks.

irrespective of the board structure used (unitary and/or a dual board structure and/or another structure) across Member States. The management body, as defined in Points (23) and (24) of Article 3(1) of Directive (EU) 2019/2034, should be understood as having management (executive) and supervisory (non-executive) functions[10].

11. The terms 'management body in its management function' and 'management body in its supervisory function' are used throughout these guidelines without referring to any specific governance structure, and references to the management (executive) or supervisory (non-executive) function should be understood as applying to the bodies or members of the management body responsible for that function in accordance with national law. When implementing these guidelines, competent authorities should take into account their national company law and specify, where necessary, to which body or members of the management body those functions should apply.

12. In Member States where the management body delegates, partially or fully, the executive function to a person or an internal executive body (e.g. a chief executive officer (CEO), management team or executive committee), the persons who perform these executive functions and direct the business of the institution on the basis of that delegation should be understood as constituting the management function of the management body. For the purposes of these guidelines, any reference to the management body in its management function should be understood as also including the members of the executive body or the CEO, as defined in these guidelines, even if they have not been proposed or appointed as formal members of the investment firm's governing body or bodies under national law.

13. In Member States where some responsibilities are directly exercised by shareholders, members or owners of the investment firms instead of the management body, investment firms should ensure that such responsibilities and related decisions are in line, as far as possible, with these guidelines applicable to the management body.

14. The definitions of CEO, chief financial officer (CFO) and key function holder used in these guidelines are purely functional and are not intended to impose the appointment of those officers or the creation of such positions unless prescribed by relevant EU or national law.

Definitions

15. Unless otherwise specified, terms used and defined in Directive (EU) 2019/2034 and Regulation (EU) No 2033/2019 have the same meaning in the guidelines. In addition, for the purposes of these guidelines, the following definitions apply:

Risk appetite	means the aggregate level and types of risk that an investment firm is willing to assume within its risk capacity, in line with its business model, to achieve its strategic objectives.

[10] See also recital 27 of Directive 2019/2034/EU

Risk capacity	means the maximum level of risk an investment firm is able to assume given its capital base, its risk management and control capabilities, and its regulatory constraints.
Risk culture	means an investment firm's norms, attitudes and behaviours relating to risk awareness, risk-taking and risk management, and the controls that shape decisions on risks. The risk culture influences the decisions of management and employees during their day-to-day activities and has an impact on the risks they assume.
Staff	means all employees of an investment firm and its subsidiaries on a consolidated basis and all members of their respective management bodies in their management function and their supervisory function.
Chief executive officer (CEO)	means the person who is responsible for managing and steering the overall business activities of an investment firm.
Chief financial officer (CFO)	means the person who has the overall responsibility for managing the following activities: financial resources management, financial planning and financial reporting.
Heads of internal control functions	means the persons at the highest hierarchical level in charge of effectively managing the day-to-day operation of the independent risk management, compliance and internal audit functions.
Key function holders	means persons who have significant influence over the direction of the investment firms but who are neither members of the management body nor the CEO. They include the heads of internal control functions and the CFO, where they are not members of the management body, and, where identified on a risk-based approach by investment firms, other key function holders. Other key function holders might include heads of significant business lines, European Economic Area/European Free Trade Association branches, third country subsidiaries and other internal functions.
Union parent undertaking	means a Union parent investment firm, Union parent investment holding company or Union parent mixed financial holding company that is required to abide by the prudential requirements based on the consolidated situation in accordance with Article 7 of Regulation (EU) 2019/2033.
Prudential consolidation	means the application of the prudential rules set out in Article 25 of Directive (EU) 2019/2034 and Article 7 of Regulation (EU) 2019/2033[11]

[11] Please refer also to the RTS on the consolidation of investment firms under Directive (EU) 2019/2034

Listed investment firms	means investment firms whose financial instruments are admitted to trading on a regulated market or on a multilateral trading facility as defined under points (21) and (22) of Article 4 of Directive 2014/65/EU, in one or more Member States[12].
Shareholder	means a person who owns shares in an investment firm or, depending on the legal form of an investment firm, other owners or members of the investment firm.
Directorship	means a position as a member of the management body of an investment firm or another legal entity.

3. Implementation

Date of application

16. These guidelines apply from 30 April 2022.

[12] Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (OJ L 173, 12.6.2014, p. 349)

4. Guidelines

Title I – proportionality

17. Where applying these guidelines, competent authorities and investment firms should have regard to the principle of proportionality as set out in Article 26(3) of Directive (EU) 2019/2034 and specified further in Title I of these guidelines with a view to ensuring that the internal governance arrangements established by investment firms, including within the context of investment firm groups, are consistent with the individual risk profile of the firm and the group, commensurate with their size and internal organisation, relevant to their business model, suitable for the nature, scale and complexity of their activities and sufficient to effectively achieve the objectives of the relevant regulatory requirements and provisions.

18. For the purposes of the previous paragraph, account should be taken of the variety of different business models under which investment firms and investment firm groups operate, indicatively as investment advisors, portfolio managers, trading venues, custodians, execution or wholesale brokers, trading firms, and others. Accordingly, for the internal governance arrangements to be deemed to be consistent with the individual risk profile of the firm and the group, commensurate with their size and internal organisation, relevant to their business model, suitable for the nature, scale and complexity of their activities and sufficient to effectively achieve the objectives of the relevant regulatory requirements and provisions, it should be ensured that investment firms with a more complex organisation or with a larger scale should have more sophisticated governance arrangements, while investment firms with a simpler organisation or with a smaller scale may implement simpler governance arrangements. Investment firms should, however, note that the size or systemic importance of an investment firm may not, in itself, be indicative of the extent to which an investment firm is exposed to risks.

19. Where applying the principle of proportionality as set out in Article 26 (3) of Directive (EU) 2019/2034 and specified further in paragraph 20 of these guidelines, competent authorities and investment firms should ensure that such application does not result in the regulatory requirements being waived for investment firms or being applied in a way that means robust governance arrangements, a clear organisational structure, adequate internal control mechanisms, sound and effective risk management and appropriate remuneration policies are not ensured.

20. For the purpose of the application of the principle of proportionality and in order to ensure the appropriate implementation of the regulatory requirements and of these guidelines, the following aspects should be taken into account by investment firms and competent authorities:

a. the size in terms of the balance sheet of the investment firm and its subsidiaries within the scope of prudential consolidation;

b. whether the value of the investment firm's on and off-balance sheet assets is on average equal to or less than EUR 100 million over the four-year period immediately preceding the given financial year in accordance with the criteria set out in point (a) of Article 32(4) of Directive (EU) 2019/2034;

c. the assets under management;

d. whether the investment firm is authorised to hold client money or assets;

e. the assets safeguarded and administered;

f. the volume of client orders handled;

g. the volume of daily trading flows;

h. the geographical presence of the investment firm and the size of its operations in each jurisdiction, including in third-country jurisdictions;

i. the legal form of the investment firm, including whether the investment firm is part of a group and, if so, the proportionality assessment for the group;

j. whether it is a listed investment firm;

k. whether the investment firm is authorised to use internal models for the measurement of capital requirements (e.g. the Internal Ratings Based Approach);

l. the type of authorised activities, the services performed by the investment firm (e.g. Sections A and B of Annex I to Directive 2014/65/EU) and other services (e.g. clearing services) performed by the investment firm;

m. the underlying business model and strategy; the nature and complexity of the business activities, and the investment firm's organisational structure;

n. the risk strategy, risk appetite and actual risk profile of the investment firm, also taking into account the result of the SREP capital and SREP liquidity assessments;

o. the ownership and funding structure of the investment firm;

p. the type of clients;

q. the complexity of the financial instruments or contracts;

r. the outsourced functions and distribution channels; and

s. the existing information technology (IT) systems, including business continuity systems and outsourced functions in this area.

21. Investment firms that are legal persons managed by a single natural person should have alternative arrangements in place which ensure the sound and prudent management of such investment firms and the adequate consideration of internal governance arrangements.

Title II – role and composition of the management body and committees

1 Role and responsibilities of the management body

22. The management body must have ultimate and overall responsibility for the investment firm and defines, oversees and is accountable for the implementation of the governance arrangements as referred to in particular under Articles 26, 28 and 29 of Directive (EU) 2019/2034, within the investment firm that ensure the effective and prudent management of the investment firm.

23. The duties of the management body should be clearly defined, distinguishing between the duties of the management (executive) function and of the supervisory (non-executive) function. The responsibilities and duties of the management body should be described in a written document and duly approved by the management body. All members of the management body should be fully aware of the structure and responsibilities of the management body, and of the division of tasks between different functions of the management body and its committees, where appropriate.

24. The management body in its supervisory function and its management function should interact effectively. Both functions should provide each other with sufficient information to allow them to perform their respective roles. In order to have appropriate checks and balances in place, decision-making within the management body should not be dominated by a single member or a small subset of its members.

25. Without prejudice to the tasks and responsibilities assigned to the management body under Directive (EU) 2014/65, the management body's responsibilities should include setting, approving and overseeing the implementation of:

   a. the overall business strategy and the key policies of the investment firm within the applicable legal and regulatory framework, taking into account the investment firm's long-term financial interests and solvency;

   b. the overall risk strategy, including the investment firm's risk appetite and its risk management framework, including adequate policies and procedures, taking into

account the macroeconomic environment and the business cycle of the investment firm and measures to ensure that the management body devotes sufficient time to risk management issues; an adequate and effective internal governance and internal control framework that includes a clear organisational structure and well-functioning internal control mechanisms. Such mechanisms should include a permanent and effective compliance function and, where appropriate and proportionate in accordance with Title I, internal risk management and internal audit functions that have sufficient authority, stature and resources to perform their functions independently, and ensure compliance with applicable regulatory requirements in the context of the prevention of money laundering and terrorism financing; and also targets for the liquidity management of the investment firm;

c. a remuneration policy that is in line with the remuneration principles set out in Articles 26 and 30 to 33 of Directive (EU) 2019/2034 and the EBA guidelines on sound remuneration policies under Directive (EU) 2019/2034[13];

d. arrangements that aim to ensure that the individual and collective suitability assessments of the management body are carried out effectively, that the composition and succession planning of the management body are appropriate, and that the management body performs its functions effectively[14];

e. a selection and suitability assessment process for key function holders[15];

f. arrangements that aim to ensure the internal functioning of each committee of the management body, where established, detailing the:

    i. role, composition and tasks of each of them;

    ii. appropriate information flows, including the documentation of recommendations and conclusions, and reporting lines between each committee and the management body, competent authorities and other parties;

g. a risk culture in line with Section 8 of these guidelines that addresses the investment firm's risk awareness and risk-taking behaviour;

h. a corporate culture and values in line with Section 9 that foster responsible and ethical behaviour, including a code of conduct or similar instrument;

[13] EBA guidelines on sound remuneration policies under the IFD

[14] See also the joint ESMA and EBA guidelines on the assessment of the suitability of members of the management body and key function holders.

[15] See also the joint ESMA and EBA guidelines on the assessment of the suitability of members of the management body and key function holders.

i. a conflict of interest policy at the investment firm level in line with Section 10; and for staff in line with Section 11; and

j. arrangements that aim to ensure the integrity of the accounting and financial reporting systems, including financial and operational controls and compliance with the law and relevant standards.

26. When setting up, approving and overseeing the implementation of the aspects listed in paragraph 25, the management body should aim to ensure a business model and governance arrangements – including a risk management framework – that take into account the risks investment firms are or might be exposed to or the risks that they pose or might pose to others[16]. When taking into account all risks, investment firms should take into account all relevant risk factors, including environmental, social and governance risks factors. Investment firms should consider that the latter may drive their prudential risks[17]. Such ESG risk factors include, e.g. legal risks in the area of contractual or labour law, risks relating to potential human rights violations or other ESG risk factors that may affect the country where a service provider is located and its ability to provide the agreed service levels.

27. The management body should oversee the process of disclosure and communications with external stakeholders and competent authorities.

28. All members of the management body should be informed about the overall activity, financial and risk situation of the investment firm, taking into account the economic environment, and also about any decisions taken that have a major impact on the investment firm's business.

29. A member of the management body may be responsible for an internal control function as referred to in Title V, Section 18.1, provided that the member does not have other mandates that would compromise the member's internal control activities and the independence of the internal control function.

30. The management body should monitor, periodically review and address any weaknesses identified regarding the implementation of processes, strategies and policies relating to the responsibilities listed in paragraphs 25 and 26. The internal governance framework and its implementation should be reviewed and updated on a periodic basis, taking into account the proportionality principle, as further explained in Title I. A deeper review should be carried out where material changes affect the investment firm.

31. Where investment firms are legal persons managed by a single natural person in accordance with their constitutive rules and national laws, the references in these guidelines to a management body should be construed as applying to the single person that is responsible for

[16] See Article 26 of Directive (EU) 2019/2034.

[17] See EBA discussion paper on ESG risk management and supervision published under the CRD Art. 98(8) for a description of the EBA's understanding of ESG risks, transmission channels and recommendations for arrangements, processes, mechanisms and strategies to be implemented by institutions to identify, assess and manage ESG risks.

implementing alternative arrangements to ensure the sound and prudent management of such an investment firm and the adequate consideration of internal governance arrangements.

2 Management function of the management body

32. In its management function, the management body should actively engage in the business of an investment firm and should take decisions on a sound and well-informed basis.

33. In its management function, the management body should be responsible for the implementation of the strategies set out by the management body and regularly discuss the implementation and appropriateness of these strategies with the management body in its supervisory function. The operational implementation may be carried out by the investment firm's management.

34. In its management function, the management body should constructively challenge and critically review propositions, explanations and information received when exercising its judgement and taking decisions. In its management function, the management body should comprehensively report to, and inform regularly and where necessary without undue delay, the management body in its supervisory function of the relevant elements for the assessment of a situation, the risks and developments affecting or that may affect the investment firm, e.g. material decisions on business activities and risks taken, the evaluation of the investment firm's economic and business environment, liquidity and sound capital base, and assessment of its material risk exposures.

35. Without prejudice to the national transposition of Directive (EU) 2015/849 Anti-Money Laundering Directive (AMLD), the management body should identify one of its members in line with the requirements under Article 46(4) of Directive (EU) 2015/849 to be responsible for the implementation of the laws, regulations and administrative provisions necessary to comply with this directive, including the corresponding AML/CFT policies and procedures in the institution and at the level of the management body .

3 Supervisory function of the management body

36. The role of the members of the management body in its supervisory function should include monitoring and constructively challenging the strategy of the investment firm.

37. Without prejudice to national law, in its supervisory function the management body should include independent members as provided for in Section 9.3 of the joint ESMA and EBA guidelines on the assessment of the suitability of members of the management body and key function holders under Directive (EU) 2013/36 and Directive (EU) 2014/65.

38. Without prejudice to the responsibilities assigned under the applicable national company law, in its supervisory function the management body should:

a. oversee and monitor management decision-making and actions and provide effective oversight of the management body in its management function, including monitoring and scrutinising its individual and collective performance and the implementation of the investment firm's strategy and objectives;

b. constructively challenge and critically review proposals and information provided by members of the management body in its management function, as well as its decisions;

c. appropriately fulfil the duties and role of the risk committee and the remuneration committee, where no such committees have been set up;

d. ensure and periodically assess the effectiveness of the investment firm's internal governance framework and take appropriate steps to address any identified deficiencies;

e. oversee and monitor that the investment firm's strategic objectives, organisational structure and risk strategy, its risk appetite and risk management framework, as well as other policies (e.g. remuneration policy) and the disclosure framework are implemented consistently;

f. monitor that the risk culture of the investment firm is implemented consistently;

g. oversee the implementation and maintenance of a code of conduct or similar code and effective policies to identify, manage and mitigate actual and potential conflicts of interest;

h. oversee the integrity of financial information and reporting, and the internal control framework, including an effective and sound risk management framework;

i. ensure that the heads of internal control functions are able to act independently and, regardless of the responsibility to report to other internal bodies, business lines or units, can raise concerns and warn the management body in its supervisory function directly, where necessary, when adverse risk developments affect or may affect the investment firm; and

j. monitor the implementation of the internal audit plan following the prior involvement of the risk committee, where established.

4 Role of the chair of the management body

39. The chair of the management body should lead the management body, contribute to an efficient flow of information within the management body and between the management body and its committees, where established, and should be responsible for its effective overall functioning.

40. The chair should encourage and promote open and critical discussion and ensure that dissenting views can be expressed and discussed within the decision-making process.

41. Where the chair is permitted to assume executive duties, the investment firm should have measures in place to mitigate any adverse impact on the investment firm's checks and balances (e.g. by designating a lead board member or a senior independent board member, or by having a larger number of non-executive members within the management body in its supervisory function). The chair of the management body in its supervisory function at an investment firm must not simultaneously exercise the functions of a CEO within the same investment firm, unless justified by the investment firm and authorised by competent authorities.

42. The chair should set meeting agendas and ensure that strategic issues are discussed as a priority. He or she should ensure that decisions of the management body are taken on a sound and well-informed basis and that documents and information are received in enough time before the meeting.

43. The chair of the management body should contribute to a clear allocation of duties between members of the management body and the existence of an efficient flow of information between them in order to allow the members of the management body in its supervisory function to constructively contribute to discussions and to cast their votes on a sound and well-informed basis.

5 Committees of the management body in its supervisory function

5.1 Setting up committees

44. In accordance with Article 28 of the IFD and unless otherwise specified by national law,[18] investment firms where the value of their on and off-balance sheet assets is on average more than EUR 100 million over the four-year period immediately preceding the given financial year must establish risk and remuneration committees to advise the management body in its supervisory function and to prepare the decisions to be taken by this body.

45. Where no risk committee is established, the references in these guidelines to this committee should be construed as referring to the management body in its supervisory function.

46. Investment firms may, taking into account the criteria set out in Title I of these guidelines, establish other committees (e.g. anti-money laundering/counter terrorist financing (AML/CTF), ethics, conduct and compliance committees).

[18] Article 28 of Directive (EU) 2019/2034 requires investment firms that do not meet the criteria set out in point (a) of Article 32(4) to establish a risk committee composed of members of the management body who do not perform any executive function in the investment firm concerned.

47. Investment firms should ensure a clear allocation and distribution of duties and tasks between specialised committees of the management body. Each committee should have a documented mandate, including the scope of its responsibilities, by the management body in its supervisory function and establish appropriate working procedures.

48. Committees should support the supervisory function in specific areas and facilitate the development and implementation of a sound internal governance framework. Delegating to committees should not in any way release the management body in its supervisory function from collectively fulfilling its duties and responsibilities.

5.2 Composition of committees[19]

49. All committees should be chaired by a non-executive member of the management body who is able to exercise objective judgement.

50. Independent members[20] of the management body in its supervisory function should be actively involved in committees.

51. Where committees have to be set up in accordance with Directive (EU) 2019/2034 or national law, as a general principle they should be composed as a general principle of at least three members and have at least one independent member, taking into account the criteria set out in Title I of these guidelines and the joint EBA and ESMA guidelines on the assessment of the suitability of members of the management body and key function holders. Where there is not a sufficient number of members within the management body in its supervisory function to ensure a sound composition of committees as set out in this section, the tasks of the committee may be delegated to one member of the management body in its supervisory function, who is supported as appropriate by staff. Committees may be composed of the same group of members, taking into account the criteria set out in Title I and the number of independent members of the management body in its supervisory function alongside the specific experience, knowledge and skills that are individually or collectively required for the committees. The reasoning for the composition of committees should be documented.

52. The risk committee should be composed of non-executive members of the management body in its supervisory function of the investment firm concerned. The remuneration committee should be composed in accordance with Section 2.3 of the EBA guidelines on sound remuneration policies[21].

53. The risk committee should be chaired, where possible, by an independent member. Members of the risk committee should have, individually and collectively, appropriate knowledge, skills and expertise concerning, respectively, the selection process and suitability requirements as well as risk management and control practices. In all investment firms, the chair of the risk

[19] This section should be read in conjunction with the joint ESMA and EBA guidelines on the assessment of the suitability of members of the management body and key function holders under Directive (EU) 2013/36 and Directive (EU) 2014/65.

[20] As defined in Section 9.3 of the joint ESMA and EBA guidelines on the assessment of the suitability of members of the management body and key function holders under Directive (EU) 2013/36 and Directive (EU) 2014/65

[21] EBA guidelines on sound remuneration policies under Article 34 (3) of Directive (EU) 2019/2034

committee should, where possible, neither be the chair of the management body nor the chair of any other committee.

5.3 Committees' processes

54. Committees should regularly report to the management body in its supervisory function.

55. Committees should interact with each other as appropriate. Without prejudice to paragraph 51, such interaction could take the form of cross-participation, so that the chair or a member of a committee may also be a member of another committee.

56. Members of committees should engage in open and critical discussions, during which dissenting views are discussed in a constructive manner.

57. Committees should document the agendas of committee meetings and their main results and conclusions.

58. The risk committee should at least:

    a. have access to all the relevant information and data necessary to perform its role, including information and data from relevant corporate and control functions (e.g. legal, finance, human resources, IT, internal audit, risk and compliance, including information on AML/CTF compliance and aggregated information on suspicious transaction reports, and ML/TF risk factors);

    b. receive regular reports, ad hoc information, communications and opinions from heads of internal control functions concerning the current risk profile of the investment firm, its risk culture and its risk limits, as well as on any material breaches[22] that may have occurred, with detailed information on and recommendations for corrective measures taken, to be taken or suggested to address them; periodically review and decide on the content, format and frequency of the information regarding risk to be reported to it; and

    c. where necessary, ensure the proper involvement of the internal control functions and other relevant functions (human resources, legal and finance) within their respective areas of expertise and/or seek external expert advice.

5.4 Role of the risk committee

59. Where established, the risk committee should at least:

[22] With regard to serious breaches in the area of AML/TF, please refer also to the guidelines to be issued under Article 117 (6) of Directive 2013/36/EU, specifying the manner of cooperation and information exchange between the authorities referred to in paragraph 5 of this Article, particularly in relation to cross-border groups and in the context of identifying serious breaches of anti-money laundering rules.

a. advise and support the management body in its supervisory function with regard to the investment firm's overall current and future risk strategy and risk appetite, and assist the management body in overseeing the implementation of that strategy, to ensure that they are in line with the business objectives, corporate culture and values of the investment firm;

b. assist the management body in its supervisory function in overseeing the implementation of the investment firm's risk strategy and setting the corresponding limits;

c. oversee the implementation of the strategies for capital and liquidity management as well as for all other relevant risks of an investment firm, such as risks to clients, risks to the market, risks to firms, operational risk (including legal and IT risks) and reputational risk in order to assess their adequacy against the approved risk strategy and risk appetite;

d. provide the management body in its supervisory function with recommendations for necessary adjustments to the risk strategy resulting from, inter alia, changes to the business model of the investment firm, market developments or recommendations made by the risk management function;

e. provide advice on the appointment of external consultants that the supervisory function may decide to engage for advice or support;

f. review a number of possible scenarios, including stressed scenarios, to assess how the investment firm's risk profile would react to external and internal events;

g. oversee the alignment between all material financial instruments and services offered to clients and the business model and risk strategy of the investment firm. The risk committee, where established, should assess the risks associated with the financial instruments and services offered and take into account the alignment between the prices assigned to and the profits gained from those products and services; and

h. assess the recommendations of internal or external auditors and follow up on the appropriate implementation of measures taken.

60. The risk committee should collaborate with other committees whose activities may have an impact on the risk strategy (e.g. the remuneration committee, where established) and regularly communicate with the investment firm's internal control functions, in particular the risk management function.

Title III – governance framework

6 Organisational framework and structure

6.1 Organisational framework

61. The management body of an investment firm should ensure a suitable and transparent organisational and operational structure for that investment firm and should have a written description of it. The structure should promote and demonstrate the effective and prudent management of an investment firm at the individual and consolidated levels.

62. The management body should ensure that the internal control functions have the appropriate financial and human resources as well as powers to effectively perform their role. As a minimum, the compliance function should operate independently, including that there is an appropriate segregation of duties. The reporting lines and the allocation of responsibilities, in particular among key function holders, within an investment firm should be clear, well-defined, coherent, enforceable and duly documented. The documentation should be updated as appropriate.

63. The structure of the investment firm should not impede the ability of the management body to oversee and manage effectively the risks the investment firm or the group faces or the ability of the competent authority to effectively supervise the investment firm.

64. The management body should assess whether and how material changes to the group's structure (e.g. setting up of new subsidiaries, mergers and acquisitions, selling or winding-up parts of the group, or external developments) impact on the soundness of the investment firm's organisational framework. Where weaknesses are identified, the management body should make any necessary adjustments swiftly.

6.2 Know your structure

65. The management body should fully know and understand the legal, organisational and operational structure of the investment firm ('know your structure') and ensure that it is in line with its approved business and risk strategy and risk appetite and covered by its risk management framework

66. The management body should be responsible for the approval of sound strategies and policies for the establishment of new structures. Where an investment firm creates many legal entities within its group, their number and, in particular, the interconnections and transactions between them should not pose challenges for the design of its internal governance, nor for the effective management and oversight of the risks of the group as a whole. The management body should ensure that the structure of an investment firm and, where applicable, the structures within a group, taking into account the criteria specified in Section 7, are clear, efficient and transparent to the investment firm's staff, shareholders and other stakeholders and to the competent authority.

67. The management body should guide the investment firm's structure, its evolution and its limitations and should ensure that the structure is justified and efficient and does not involve undue or inappropriate complexity.

68. The management body of a Union parent undertaking should understand not only the legal, organisational and operational structure of the group, but also the purpose and activities of its different entities and the links and relationships among them. This includes understanding group-specific operational risks and intra-group exposures as well as how the group's funding, capital, liquidity and risk profiles could be affected under normal and adverse circumstances. The management body should ensure that the parent investment firm is able to produce information on the group in a timely manner regarding the type, characteristics, organisational chart, ownership structure and businesses of each legal entity, and that the investment firms within the group comply with all the supervisory reporting requirements on an individual and consolidated basis.

69. The management body of a Union parent undertaking should ensure that the different group entities (including the Union parent undertaking itself) receive enough information to have a clear understanding of the general objectives, strategies and risk profile of the group and how the group entity concerned is embedded into the group's structure and operational functioning. Such information – and any revisions thereof – should be documented and made available to the relevant functions concerned, including the management body, business lines and internal control functions. The members of the management body of a Union parent undertaking should keep themselves informed about the risks the group's structure causes, taking into account the criteria specified in Section 7 of the guidelines. This includes receiving:

    a. information on major risk drivers;

    b. regular reports assessing the investment firm's overall structure and evaluating the compliance of individual entities' activities with the approved group-wide strategy; and

    c. regular reports on topics where the regulatory framework requires compliance at the individual and consolidated levels.

6.3 Complex structures and non-standard or non-transparent activities

70. Investment firms should avoid setting up complex and potentially non-transparent structures. Investment firms should take into account in their decision-making the results of a risk assessment performed to identify whether such structures could be used for a purpose connected with money laundering, terrorist financing or other financial crimes and the

respective controls and legal framework in place[23]. To this end, investment firms should take into account, as a minimum:

a. the extent to which the jurisdiction in which the structure will be set up complies effectively with EU and international standards on tax transparency, anti-money laundering and countering the financing of terrorism[24];

b. the extent to which the structure serves an obvious economic and lawful purpose;

c. the extent to which the structure could be used to hide the identity of the ultimate beneficial owner;

d. the extent to which the customer's request that leads to the possible setting-up of a structure gives rise to concern;

e. whether the structure might impede appropriate oversight by the investment firm's management body or the investment firm's ability to manage the related risk; and

f. whether the structure poses obstacles to effective supervision by competent authorities.

71. In any case, investment firms should not set up opaque or unnecessarily complex structures that have no clear economic rationale or legal purpose, or structures that could raise concerns that these might be created for a purpose connected with financial crime.

72. When setting up such structures, the management body should understand them and their purpose and the particular risks associated with them and ensure that the internal control functions are appropriately involved. Such structures should be approved and maintained only when their purpose has been clearly defined and understood, and when the management body is satisfied that all material risks, including reputational risks, have been identified, that all risks can be managed effectively and appropriately reported, and that effective oversight has been ensured. The more complex and opaque the organisational and operational structure, and the greater the risks, the more intensive the oversight of the structure should be.

73. Investment firms should document their decisions and be able to justify their decisions to competent authorities.

[23] For further details on the assessment of country risk and the risk associated with individual products and customers, investment firms should also refer to the joint guidelines on ML/TF risk factors (EBA GL JC/2017/37) currently under review.

[24] See also Commission Delegated Regulation (EU) 2019/758 of 31 January 2019 supplementing Directive (EU) 2015/849 of the European Parliament and of the Council with regard to regulatory technical standards for the minimum action and the type of additional measures credit and financial institutions must take to mitigate money laundering and terrorist financing risk in certain third countries: https://eba.europa.eu/regulation-and-policy/anti-money-laundering-and-e-money/rts-on-the-implementation-of-group-wide-aml/cft-policies-in-third-countries

74. The management body should ensure that appropriate actions are taken to avoid or mitigate the risks of activities within such structures. This includes ensuring that:

    a. the investment firm has in place adequate policies and procedures and documented processes (e.g. applicable limits and information flows) for the consideration, compliance, approval and risk management of such activities, taking into account the consequences for the group's organisational and operational structure, its risk profile and its reputational risk;

    b. information concerning these activities and the risks thereof is accessible to the Union parent undertaking as well as internal and external auditors and is reported to the management body in its supervisory function and to the competent authority that granted authorisation; and

    c. the investment firm periodically assesses the continuing need to maintain such structures.

75. These structures and activities, including their compliance with legislation and professional standards, should be subject to a regular review. Where an internal audit function is established, it should perform the review on a risk-based approach.

76. Investment firms should take effective risk management measures when they perform non-standard or non-transparent activities for clients (e.g. helping clients to set up vehicles in offshore jurisdictions, developing complex structures, facilitating transactions for them or providing trustee services) that pose similar internal governance challenges and create significant operational and reputational risks. In particular, investment firms should analyse the reason why a client wants to set up a particular structure.

7 Organisational framework in a group context

77. In accordance with Article 25 of Directive (EU) 2019/2034 and Article 7 of Regulation (EU) 2019/2033, and unless Article 8 of Regulation (EU) 2019/2033 is applied by competent authorities, Union parent undertakings and their subsidiaries subject to Directive (EU) 2019/2034 should ensure that governance arrangements, processes and mechanisms are consistent and well integrated on a consolidated basis. To this end, undertakings and subsidiaries within the scope of prudential consolidation should implement such arrangements, processes and mechanisms in their subsidiaries not subject to Directive (EU) 2019/2034, including those established in third countries including in offshore financial centres – to ensure robust governance arrangements on a consolidated basis. Competent functions within the Union parent undertaking and its subsidiaries should interact and exchange data and information as appropriate. The governance arrangements, processes and mechanisms should ensure that the Union parent undertaking has sufficient data and information and is able to assess the group-wide risk profile as detailed in Section 6.2.

78. The management body of a subsidiary that is subject to Directive (EU) 2019/2034 should adopt and implement at the individual level the group-wide governance policies established at the consolidated level, in a manner that complies with all the specific requirements under EU and national law.

79. At the consolidated level, the Union parent undertaking should ensure adherence to the group-wide governance policies and internal control framework as referred to in Title V by all investment firms and other entities within the scope of prudential consolidation, including its subsidiaries not themselves subject to Directive (EU) 2019/2034. When implementing governance policies, the Union parent undertaking should ensure that robust governance arrangements are in place for each subsidiary and consider specific arrangements, processes and mechanisms where business activities are organised not in separate legal entities but within a matrix of business lines that encompasses multiple legal entities.

80. A Union parent undertaking should consider the interests of all its subsidiaries, and how strategies and policies contribute to the interests of each subsidiary and the interests of the group as a whole over the long term.

81. A Union parent undertaking and its subsidiaries should ensure that the investment firms and entities within the group comply with all the specific regulatory requirements in any relevant jurisdiction.

82. The Union parent undertaking should ensure that subsidiaries established in third countries that are included in the scope of prudential consolidation have governance arrangements, processes and mechanisms in place that are consistent with group-wide governance policies and comply with the requirements of Articles 25 to 32 of Directive (EU) 2019/2034 and these guidelines, as long as this is not unlawful under the laws of the third country.

83. The governance requirements of Directive 2019/2034/EU and the provisions in these guidelines apply to investment firms located in the EU independent of the fact that they may be subsidiaries of a parent undertaking in a third country. Where an EU subsidiary of a parent undertaking in a third country is a Union parent undertaking, the scope of prudential consolidation within the EU does not include the level of the parent investment firm located in a third country and other direct subsidiaries of that parent undertaking. The Union parent undertaking should ensure that the group-wide governance policy of the parent investment firm in a third country is taken into consideration within its own governance policy insofar as this is not contrary to the requirements set out under relevant EU law, including Directive (EU) 2019/2034 and the additional specifications under these guidelines.

84. When establishing policies and documenting governance arrangements, investment firms should take into account the aspects listed in Annex I. While policies and documentation may be included in separate documents, investment firms should consider combining them or referring to them in a single governance framework document.

Title IV – risk culture and business conduct

8 Risk culture

85. A sound, diligent and consistent risk culture should be a key element of investment firms' effective risk management and should enable investment firms to make sound and informed decisions.

86. Investment firms should develop an integrated and investment firm-wide risk culture, based on a full understanding and holistic view of the risks they face including the risks to clients, to markets, the risk to the investment firm itself and the liquidity risks, in particular those which can have a material impact on or deplete the level of own funds available and how they are managed, taking into account the investment firm's risk capacity and risk appetite.

87. Investment firms should develop a risk culture through policies, communication and staff training regarding the investment firms' activities, strategy and risk profile, and should adapt communication and staff training to take into account staff's responsibilities regarding risk-taking and risk management.

88. Staff should be fully aware of their responsibilities relating to risk management. Risk management should not be confined to risk specialists or internal control functions. Business units, under the oversight of the management body, should be primarily responsible for managing risks on a day-to-day basis in line with the investment firm's policies, procedures and controls, taking into account the investment firm's risk appetite and risk capacity.

89. A strong risk culture should include but is not necessarily limited to:

    a. Tone from the top: the management body should be responsible for setting and communicating the investment firm's core values and expectations. The behaviour of its members should reflect these values. Investment firms' management, including key function holders, should contribute to the internal communication of core values and expectations to staff. Staff should act in accordance with all applicable laws and regulations and promptly escalate observed non-compliance within or outside the investment firm (e.g. to the competent authority through a whistleblowing process). The management body should, on an ongoing basis, promote, monitor and assess the risk culture of the investment firm, consider the impact of the risk culture on the financial stability, risk profile and robust governance of the investment firm and make changes where necessary.

    b. Accountability: relevant staff at all levels should know and understand the core values of the investment firm and, to the extent necessary for their role, its risk appetite and risk capacity. They should be capable of performing their roles and be aware that they will be held accountable for their actions in relation to the investment firm's risk-taking behaviour.

c. Effective communication and challenge: a sound risk culture should promote an environment of open communication and effective challenge in which decision-making processes encourage a broad range of views, allow for testing of current practices, stimulate a constructive critical attitude among staff and promote an environment of open and constructive engagement throughout the entire organisation.

d. Incentives: appropriate incentives should play a key role in aligning risk-taking behaviour with the investment firm's risk profile and its long-term interests[25].

9 Corporate values and code of conduct

90. The management body should develop, adopt, adhere to and promote high ethical and professional standards, taking into account the specific needs and characteristics of the investment firms, and should ensure the implementation of such standards (through a code of conduct or similar instrument). It should also oversee adherence to these standards by staff. Where applicable, the management body may adopt and implement the investment firm's group-wide standards or common standards released by associations or other relevant organisations.

91. Investment firms should ensure that there is no discrimination towards staff based on gender, race, colour, ethnic or social origin, genetic features, languages, religion or belief, political or any other opinion, membership of a national minority, property, birth, disability, age or sexual orientation.

92. Investment firms' policies should be gender-neutral. This includes, but is not limited to, remuneration, recruitment policies, career development and succession plans, access to training and the ability to apply for internal vacancies. Institutions should ensure equal opportunities[26] for all staff irrespective of their gender, including with regard to career perspectives, and aim to improve representation of the underrepresented gender in positions within the management body as well as in the group of staff that have managerial responsibilities as defined in the Commission's Delegated Regulation (regulatory technical standards (RTS) on identified staff). Investment firms should monitor the trend in the gender pay gap. Where investment firms have 50 or more staff[27], the monitoring should be separately for identified staff (excluding members of the management body), members of the management body in its management function, members of the management body in the supervisory function and other staff. Institutions should have policies that facilitate the reintegration of staff after maternity, paternity or parental leave.[28]

[25] Please refer also to the EBA guidelines on sound remuneration policies under Directive (EU) 2034/2019

[26] See also Directive 2006/54/EC of the European Parliament and of the Council of 5 July 2006 on the implementation of the principle of equal opportunities and equal treatment of men and women in matters of employment and occupation

[27] See also EBA Guidelines on sound remuneration policies under Directive (EU) 2019/2034

[28] See also EBA Guidelines on sound remuneration policies under Directive (EU) 2019/2034

93. The standards implemented should aim to enhance the institution's robust governance arrangements and reduceing the risk to which the investment firm is exposed, in particular operational and reputational risks, which can have a considerable adverse impact on an investment firm's profitability and sustainability through fines, litigation costs, restrictions imposed by competent authorities, other financial and criminal penalties, and the loss of brand value and consumer confidence.

94. The management body should have clear and documented policies for how these standards should be met. These policies should:

    a. remind staff that all the investment firm's activities should be conducted in compliance with the applicable law and with the investment firm's corporate values;

    b. promote risk awareness through a strong risk culture in line with Section 9 of the guidelines, conveying the management body's expectation that activities will not go beyond the defined risk appetite and limits defined by the investment firm and the respective responsibilities of staff;

    c. set out principles on and provide examples of acceptable and unacceptable behaviours linked in particular to financial misreporting and misconduct, economic and financial crime including but not limited to fraud, money laundering and terrorist financing (ML/TF), anti-trust practices, financial sanctions, bribery and corruption, market manipulation, mis-selling and other violations of consumer protection laws, tax offences, whether committed directly or indirectly, including through unlawful or banned dividend arbitrage schemes;

    d. clarify that in addition to complying with legal and regulatory requirements and internal policies, staff are expected to conduct themselves with honesty and integrity and perform their duties with due skill, care and diligence; and

    e. ensure that staff are aware of the potential internal and external disciplinary actions, legal actions and sanctions that may follow misconduct and unacceptable behaviours.

95. Investment firms should monitor compliance with such standards and ensure staff awareness, e.g. by providing training. Investment firms should define the function responsible for monitoring compliance with and evaluating breaches of the code of conduct or similar instrument and a process for dealing with issues of non-compliance. The results should periodically be reported to the management body.

10 Conflict of interest policy at firm level

96. The management body should be responsible for establishing, approving and overseeing the implementation and maintenance of effective policies to identify, assess, manage and mitigate or prevent actual and potential conflicts of interest at firm level, e.g. as a result of the various activities and roles of the investment firm, of different investment firms within the scope of

prudential consolidation or of different business lines or units within an investment firm, or with regard to external stakeholders. When setting these policies, investment firms should be aware that these policies need also to be compliant with Article 16(3) and 23 of Directive 2014/65/EU and Articles 33 to 35 of the Commission delegated regulation 2017/565.

97. Investment firms' measures to manage or where appropriate mitigate conflicts of interest should be documented and include, inter alia:

    a. an appropriate segregation of duties, e.g. entrusting conflicting activities within the processing of transactions or when providing services to different persons, or entrusting supervisory and reporting responsibilities for conflicting activities to different persons;

    b. establishing information barriers, e.g. through the physical separation of certain business lines or units.

11 Conflict of interest policy for staff[29]

98. Without prejudice to Article 23 of Directive 2014/65/EU and Section 3 of the Chapter 2 of the Commission Delegated Regulation (EU) No 2017/565, the management body should be responsible for establishing, approving and overseeing the implementation and maintenance of effective policies to identify, assess, manage and mitigate or prevent actual and potential conflicts between the interests of the investment firm and the private interests of staff, including members of the management body, which could adversely influence the performance of their duties and responsibilities. A Union parent undertaking should consider interests within a group-wide conflict of interest policy on a consolidated basis.

99. The policy should aim to identify conflicts of interest of staff, including the interests of their closest family members. Investment firms should take into consideration that conflicts of interest may arise not only from present but also from past personal or professional relationships. Where conflicts of interest arise, investment firms should assess their materiality and decide on and implement mitigating measures as appropriate.

100. Regarding conflicts of interest that may result from past relationships, investment firms should set an appropriate timeframe for which they want staff to report such conflicts of interest, on the basis that these may still have an impact on staff's behaviour and participation in decision-making.

101. The policy should cover at least the following situations or relationships where conflicts of interest may arise:

    a. economic interests (e.g. shares, other ownership rights and memberships, financial holdings and other economic interests in commercial customers, intellectual property

[29] This section should be read in conjunction with the joint ESMA and EBA guidelines on the assessment of the suitability of members of the management body and key function holders under Directive 2013/36/EU and Directive 2014/65/EU.

rights, membership of a body or ownership of a body or entity with conflicting interests);

b. personal or professional relationships with the owners of qualifying holdings in the investment firms;

c. personal or professional relationships with staff of the investment firms or entities included within the scope of prudential consolidation (e.g. family relationships);

d. other employment and previous employment within the recent past (e.g. five years);

e. personal or professional relationships with relevant external stakeholders (e.g. being associated with material suppliers, consultancies or other service providers); and

f. political influence or political relationships.

102. Notwithstanding the above, investment firms should take into consideration that being a shareholder of an investment firm or using other services of an investment firm should not lead to a situation where staff are considered to have a conflict of interest if they stay within an appropriate de minimis threshold.

103. The policy should set out the processes for reporting and communication to the function responsible under the policy. Staff should have the duty to promptly disclose internally any matter that may result, or has already resulted, in a conflict of interest.

104. The policy should differentiate between conflicts of interest that persist and need to be managed permanently and conflicts of interest that occur unexpectedly with regard to a single event (e.g. a transaction or the selection of a service provider, etc.) and can usually be managed with a one-off measure. In all circumstances, the interests of the investment firm should be central to the decisions taken.

105. The policy should set out procedures, measures, documentation requirements and responsibilities for the identification and prevention of conflicts of interest, for the assessment of their materiality and for taking mitigating measures. Such procedures, requirements, responsibilities and measures should include:

a. entrusting conflicting activities or transactions to different persons;

b. preventing staff who are also active outside the investment firm from having inappropriate influence within the investment firm regarding those other activities;

c. establishing the responsibility of the members of the management body to abstain from voting on any matter where a member has or may have a conflict of interest or

where the member's objectivity or ability to properly fulfil his or her duties to the investment firm may be otherwise compromised;

d. preventing members of the management body from holding directorships in competing investment firms.

106. The policy should specifically cover the risk of conflicts of interest at the level of the management body and provide sufficient guidance on the identification and management of conflicts of interest that may impede the ability of members of the management body to take objective and impartial decisions that aim to fulfil the best interests of the investment firms. Investment firms should take into consideration that conflicts of interest can have an impact on the independence of mind of members of the management body[30].

107. When mitigating identified conflicts of interest of members of the management body, investment firms should document the measures taken, including the reasoning on how such measures are effective in ensuring objective decision-making.

108. Actual or potential conflicts of interest that have been disclosed to the responsible function within the investment firm should be appropriately assessed and managed. If a conflict of interest of staff is identified, the investment firm should document the decision taken, in particular if the conflict of interest and the related risks have been accepted; and if it has been accepted, how this conflict of interest has been satisfactorily mitigated or remedied.

109. All actual and potential conflicts of interest at the management body level, individually and collectively, should be adequately documented, communicated to the management body and discussed, decided on and duly managed by the management body.

11.1 Conflicts of interest policy in the context of loans and other transactions with members of the management body and their related parties

110. As part of their conflicts of interest policies for staff (Section 11) and the management of conflicts of interest of members of the management body as set out in paragraph 107, the management body should set out a framework for identifying and managing conflicts of interest in the context of granting loans and entering into other transactions, e.g. initial public offerings, service agreements or outsourcing agreements with members of the management body and their related parties.

111. Investment firms should consider additional categories of related parties to whom they apply, in whole or in part, their conflicts of interest framework regarding loans and transactions.

[30] See also the joint ESMA and EBA guidelines on the assessment of the suitability of members of the management body and key function holders under Directive 2013/36/EU and Directive 2014/65/EU.

112. The conflicts of interest framework should ensure that decisions regarding loans and entering into other transactions with members of the management body and their related parties are taken objectively, without undue influence from conflicts of interest and are, as a general principle, conducted at arm's length.

113. The management body should set out the applicable decision-making processes for granting loans and entering into other transactions with members of the management body and their related parties. This framework may provide for a differentiation between standard business transactions[31] entered into in the ordinary course of business and concluded on normal market terms and staff transactions, which are concluded subject to conditions available to all staff. Furthermore, the conflicts of interest framework and decision-making process may differentiate between material and non-material loans or other material transactions, different types of loans and other transactions and the level of actual or potential conflicts of interest they may create.

114. As part of the conflicts of interest framework, the management body should set appropriate thresholds (e.g. per product type, volume, or depending on the conditions) above which the transaction with a member of the management body or its related parties always requires approval by the management body. Decisions on material loans and other material transactions with members of the management body that are not being concluded under normal market terms, but subject to conditions available to all staff, should always be made by the management body.

115. The member of the management body benefiting from such a material loan or other material transaction, or the member who is related to the counterparty, should not be involved in the decision-making process.

116. When deciding on a loan or other transaction with a member of the management body or their related parties, before taking a decision investment firms should assess the risk to which the investment firm might be exposed due to the transaction.

117. To ensure compliance with their conflicts of interest policies, investment firms should ensure that all relevant internal control procedures fully apply to loans and other transactions with members of the management body or their related parties and that an appropriate oversight framework is in place at the level of the management body in its supervisory function.

11.2 Documentation of loans to members of the management body and their related parties and additional information

[31] Business transactions include loan leasing, factoring, services in the context of initial public offerings (IPOs), mergers and acquisitions and buying and selling property.

118. For the purposes of Article 26 of Directive (EU) 2019/2034, investment firms should document data on loans to members of the management body and their related parties properly, including at least:

    a. the name of the debtor and their status (i.e. member of the management body or related party) and, with regard to loans to a related party, the member of the management body to whom the party is related and the nature of the relationship to the related party;

    b. the type/nature of loan and the amount;

    c. the terms and conditions applicable to the loan;

    d. the date of approval of the loan;

    e. the name of the individual or body and its composition taking the decision to approve the loan and the applicable conditions;

    f. the fact (yes/no) as to whether or not the loan has been granted at market conditions; and

    g. the fact (yes/no) as to whether or not the loan has been granted at conditions available to all staff.

119. Investment firms should ensure that the documentation of all loans to members of the management body and their related parties is complete and updated and that the investment firm is able to make available to competent authorities the complete documentation in an appropriate format upon request and without undue delay.

12 Internal alert procedures

120. Investment firms should put in place and maintain appropriate internal alert policies and procedures for staff to report potential or actual breaches of Regulation (EU) No 2033/2019 and national provisions transposing Directive (EU) 2019/2034 through a specific, independent and autonomous channel. It should not be necessary for reporting staff to have evidence of a breach; however, they should have a sufficient level of certainty that provides sufficient reason to launch an investigation. Investment firms should also implement appropriate processes and procedures that ensure that they comply with their obligations under the national implementation of Directive (EU) 2019/1937 of the European Parliament and of the Council of 23 October 2019 on the protection of persons who report breaches of Union law.

121. To avoid conflicts of interest, it should be possible for staff to report breaches outside regular reporting lines (e.g. through the compliance function, the internal audit function or an independent internal whistleblowing procedure). The alert procedures should ensure the

protection of the personal data of both the person who reports the breach and the natural person who is allegedly responsible for the breach, in accordance with Regulation (EU) 2016/679[32] (GDPR).

122. The alert procedures should be made available to all staff within an investment firm.

123. Information provided by staff through the alert procedures should, if appropriate, be made available to the management body and other responsible functions defined within the internal alert policy. Where required by the staff member reporting a breach, the information should be provided to the management body and other responsible functions in an anonymised way. Investment firms may also provide for a whistleblowing process that allows information to be submitted in an anonymised way.

124. Investment firms should ensure that the person reporting the breach is appropriately protected from any negative impact, e.g. retaliation, discrimination or other types of unfair treatment. The investment firm should ensure that no person under the investment firm's control engages in the victimisation of a person who has reported a breach and should take appropriate measures against those responsible for any such victimisation.

125. Investment firms should also protect persons who have been reported from any negative effects in case the investigation finds no evidence that justifies taking measures against that person. If measures are taken, the investment firms should take them in a way that aims to protect the person concerned from unintended negative effects that go beyond the objective of the measure taken.

126. In particular, internal alert procedures should:

   a. be documented (e.g. staff handbooks);

   b. provide clear rules that ensure that information on the reporting and the reported persons and the breach are treated confidentially, in accordance with Regulation (EU) 2016/679, unless disclosure is required under national law in the context of further investigations or subsequent judicial proceedings;

   c. protect staff who raise concerns from being victimised because they have disclosed reportable breaches;

   d. ensure that the potential or actual breaches raised are assessed and escalated, including as appropriate to the relevant competent authority or law enforcement agency;

[32] Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation)

e. ensure, where possible, that confirmation of receipt of information is provided to staff who have raised potential or actual breaches;

f. ensure the tracking of the outcome of an investigation into a reported breach; and

g. ensure appropriate record keeping.

13 Reporting of breaches to competent authorities

127. In accordance with article 22 of Directive (EU) 2019/2034, competent authorities should establish effective and reliable mechanisms to enable investment firms' staff to report to competent authorities relevant potential or actual breaches of Regulation (EU) No 2019/2033 and national provisions transposing Directive (EU) 2019/2034. These mechanisms should include, as a minimum:

a. specific procedures for the receipt of reports on breaches and follow-up, for instance a dedicated whistleblowing department, unit or function;

b. appropriate protection as referred to in Section 13;

c. protection of the personal data of both the natural person who reports the breach and the natural person who is allegedly responsible for the breach, in accordance with Regulation (EU) 2016/679 (GDPR); and

d. clear procedures as set out in Section 12.

128. Without prejudice to the possibility of reporting breaches through the competent authorities' mechanisms, competent authorities may encourage staff to first try and seek to use their investment firms' internal alert procedures.

Title V – internal control framework and mechanisms

14 Internal control framework

129. Investment firms should develop and maintain a culture that encourages a positive attitude towards risk control and compliance within the investment firms and a robust and comprehensive internal control framework. Under this framework, investment firms' business lines should be responsible for managing the risks they incur in conducting their activities and should have controls in place that aim to ensure compliance with internal and external requirements. As part of this framework, investment firms should have a permanent and effective internal compliance function[33] with appropriate and sufficient authority, stature and access to the management body to fulfil its mission, and a risk management framework.

[33] Without prejudice to Article 22 of the EU Commission Delegated Regulation 565/2017

Where proportionate taking into account the criteria listed in Title I, investment firms should also have an internal risk management and audit function.

130. The internal control framework of the investment firm concerned should be adapted on an individual basis to the specificity of its business, its complexity and the associated risks, taking into account the group context. The investment firm concerned should organise the exchange of the necessary information in a manner that ensures that each management body, business line and internal unit, including each internal control function, is able to carry out its duties. This means, for example, a necessary exchange of adequate information between the business lines and the compliance function, and the AML/CFT compliance function where it is a separate control function, at the group level and between the heads of the internal control functions at the group level and the management body of the investment firms.

131. Investment firms should implement appropriate processes and procedures to ensure that they comply with their obligations in the context of combating money laundering and terrorist financing. Investment firms should assess their exposure to the risk that they may be used for the purpose of ML/TF and, where necessary, take mitigating measures to reduce those risks as well as the operational and reputational risks linked to them. Investment firms should take measures to ensure that their staff are aware of such ML/TF risks and the impact that ML/TF has on the investment firm and the integrity of the financial system.

132. The internal control framework should cover the whole organisation, including the management body's responsibilities and tasks, and the activities of all business lines and internal units, including internal control functions, outsourced activities and distribution channels.

133. The internal control framework of an investment firm should ensure:

   a. effective and efficient operations;

   b. adequate identification, measurement and mitigation of risks;

   c. the reliability of financial and non-financial information reported both internally and externally;

   d. sound administrative and accounting procedures; and

   e. compliance with laws, regulations, supervisory requirements and the investment firm's internal policies, processes, rules and decisions.

15 Implementing an internal control framework

134. The management body should be responsible for establishing and monitoring the adequacy and effectiveness of the internal control framework, processes and mechanisms, and for

overseeing all business lines and internal units, including internal control functions (such as compliance including AML/CFT compliance where separate from the compliance function, and risk management and internal audit functions where established). Investment firms should establish, maintain and regularly update adequate written internal control policies, mechanisms and procedures, which should be approved by the management body. Where no risk management function is established, the management body should be responsible for establishing and monitoring adequate risk management procedures and policies.

135. An investment firm should have a clear, transparent and documented decision-making process and a clear allocation of responsibilities and authority within its internal control framework, including its business lines, internal units and internal control functions.

136. Investment firms should communicate these policies, mechanisms and procedures to all staff and every time material changes have been made.

137. The internal control functions should verify that the policies, mechanisms and procedures set out in the internal control framework are correctly implemented in their respective areas of competence.

138. Internal control functions should regularly submit to the management body written reports on major deficiencies that have been identified. These reports should include, for each new major deficiency identified, the relevant risks involved, an impact assessment, recommendations and corrective measures to be taken. The management body should follow up on the findings of the internal control functions in a timely and effective manner and require adequate remedial actions. A formal follow-up procedure on findings and corrective measures taken should be put in place.

16 Risk management framework

139. As part of the overall internal control framework, investment firms should have a holistic investment firm-wide risk management framework extending across all their business lines and internal units, including internal control functions, recognising fully the economic substance of all their risk exposures including the risks the investment firm poses to itself, its customers and markets and liquidity risks, in particular those that can have a material impact on or deplete the level of own funds available. The risk management framework should enable the investment firm to make fully informed decisions on risk-taking. The risk management framework should encompass all risks as well as actual risks and future risks that the investment firm may be exposed to. Risks should be evaluated from the bottom up and from the top down, within and across business lines, using consistent terminology and compatible methodologies throughout the investment firm and at a consolidated level. All relevant risks should be encompassed in the risk management framework with appropriate consideration given to both financial and non-financial risks, including market, liquidity, concentration, operational, IT, reputational, legal, conduct, compliance with AML/CTF and other financial crime, ESG and strategic risks.

140. An investment firm's risk management framework should include policies, procedures, risk limits and risk controls ensuring adequate, timely and continuous identification, measurement or assessment, monitoring, management, mitigation and reporting of the risks at the business line, investment firm and consolidated levels.

141. An investment firm's risk management framework should provide specific guidance on the implementation of its strategies. This guidance should, where appropriate, establish and maintain internal limits consistent with the investment firm's risk appetite and commensurate with its sound operation, financial strength, capital base and strategic goals. An investment firm's risk profile should be kept within these established limits. The risk management framework should ensure that, whenever breaches of risk limits occur, there is a defined process to escalate and address them with an appropriate follow-up procedure.

142. The risk management framework should be subject to independent internal review, e.g. performed by the internal audit function, and reassessed regularly against the investment firm's risk appetite, taking into account information from the risk management function and the risk committee, where established. Factors that should be considered include internal and external developments, including revenue changes; any increase in the complexity of the investment firm's business, risk profile or operating structure; geographic expansion; mergers and acquisitions; and the introduction of new products or business lines.

143. When identifying and measuring or assessing risks, an investment firm should develop appropriate methodologies including both forward-looking and backward-looking tools. The tools should include the assessment of the actual risk profile against the investment firm's risk appetite, as well as the identification and assessment of potential and stressed risk exposures under a range of assumed adverse circumstances against the investment firm's risk capacity. The tools should provide information on any adjustment to the risk profile that may be required. Investment firms should make appropriately conservative assumptions when building stressed scenarios.

144. Investment firms should take into consideration that the results of quantitative assessment methodologies, including stress testing, are highly dependent on the limitations and assumptions of the models (including the severity and duration of the shock and the underlying risks). For example, models showing very high returns on economic capital may result from a weakness in the models (e.g. the exclusion of some relevant risks) rather than a superior strategy or excellent execution of a strategy on the part of the investment firm. The determination of the level of risk taken should not therefore be based only on quantitative information or model outputs; it should also comprise a qualitative approach (including expert judgement and critical analysis). Relevant macroeconomic environmental trends and data should be explicitly addressed to identify their potential impact on exposures and portfolios.

145. The ultimate responsibility for risk assessment lies solely with the investment firm, which, accordingly, should evaluate its risks critically and should not rely exclusively on external assessments.

146. Investment firms should be fully aware of the limitations of models and metrics and use not only quantitative but also qualitative risk assessment tools (including expert judgement and critical analysis).

147. In addition to the investment firms' own assessments, investment firms may use external risk assessments (including external credit ratings or externally purchased risk models). Investment firms should be fully aware of the exact scope of such assessments and their limitations.

148. Regular and transparent reporting mechanisms should be established so that the management body, its risk committee, where established, and all relevant units in an investment firm are provided with reports in a timely, accurate, concise, understandable and meaningful manner and can share relevant information about the identification, measurement or assessment, monitoring and management of risks. The reporting framework should be well defined and documented.

149. Effective communication and awareness regarding risks and the risk strategy is crucial for the whole risk management process, including the review and decision-making processes, and helps prevent decisions that may unknowingly increase risk. Effective risk reporting involves sound internal consideration and the communication of the risk strategy and relevant risk data (e.g. exposures and key risk indicators), both horizontally across the investment firms and up and down the management chain.

17 Internal control functions

150. The internal control functions should include an effective and permanent internal compliance function, and where appropriate and proportionate, taking into account the criteria listed in Title I, a risk management function and an internal audit function. The responsibilities of control functions also include ensuring compliance with AML/CTF requirements. Where investment firms do not establish and maintain a risk management function and an internal audit function, they should be able to demonstrate upon request that the policies and procedures adopted and implemented for an internal control framework effectively achieve the same outcome as the guidelines provided in this Title V.

151. Where the investment firm does not establish an internal risk management function (RMF) or internal audit function (IAF), the responsibilities of these functions as set out in these guidelines are with the staff in charge of the established procedures and ultimately the management body, who may delegate the operational tasks internally or externally.

152. Without prejudice to national law implementing Directive (EU) 2015/849, institutions should assign the responsibility for ensuring the institution's compliance with the requirements of that directive and the institution's policies and procedures to a staff member (e.g. head of compliance). Institutions may establish a separate AML/CTF compliance function as an independent control function. The person responsible for AML/CTF should, where necessary, be able to report directly to the management body in its management and its supervisory function.

17.1 Heads of the internal control functions

153. Heads of internal control functions should be established at an adequate hierarchical level that provides the head of the control function with the appropriate authority and stature needed to fulfil his or her responsibilities. The head of compliance and, where established, the heads of the risk management and internal audit functions should report and be directly accountable to the management body, and their performance should be reviewed by the management body.

154. Where necessary, the heads of internal control functions should be able to have access and report directly to the management body in its supervisory function to raise concerns and warn the supervisory function, where appropriate, when specific developments affect or may affect the investment firms. This should not prevent the heads of internal control functions from reporting within the regular reporting lines as well.

155. Investment firms should have documented processes in place to assign the position of the head of an internal control function and for withdrawing his or her responsibilities. In any case, the heads of internal control functions should not be removed without the prior approval of the management body in its supervisory function.

17.2 Independence of internal control functions

156. In order for the internal control functions to be regarded as operating independently, the following conditions should be met:

    a. their staff do not perform any operational tasks that fall within the scope of the activities the internal control functions are intended to monitor and control unless it is demonstrated that, in view of the criteria listed in Title I for the application of the proportionality principle, the internal control functions continue to be effective. In that case, investment firms should assess whether the effectiveness of their internal control functions is compromised.

    b. Where appropriate, they are organisationally separate from the activities they are assigned to monitor and control;

    c. the remuneration of the internal control functions staff should not be linked to the performance of the activities the internal control function monitors and controls, and should not otherwise be likely to compromise the staff members' objectivity[34].

17.3 Resources of internal control functions

[34] See also the EBA guidelines on sound remuneration policies, available at https://www.eba.europa.eu/regulation-and-policy/remuneration/guidelines-on-sound-remuneration-policies.

157. Internal control functions should have sufficient resources. Taking into account the application of the proportionality principle as set out in Title I, they should have an adequate number of qualified staff (at both the parent and subsidiary levels). Staff should remain qualified on an ongoing basis and should receive training as necessary.

158. Internal control functions should have appropriate IT systems and support at their disposal, with access to the internal and external information necessary to meet their responsibilities. They should have access to all necessary information regarding all business lines and relevant risk-bearing subsidiaries, in particular those that can potentially generate material risks for the investment firm.

18 Risk management function

159. The risk management function (RMF) should cover the whole investment firm. The RMF should have sufficient authority, stature and resources, taking into account the proportionality criteria listed in Title I, to implement risk policies and the risk management framework as set out in Section 17.

160. The RMF should have, where necessary, direct access to the management body in its supervisory function and its committees, where established, including in particular the risk committee.

161. The RMF should have access to all business lines and other internal units that have the potential to generate risk, as well as to relevant subsidiaries and affiliates.

162. Staff within the RMF should possess sufficient knowledge, skills and experience in relation to risk management techniques and procedures, and markets and products, and should have access to regular training.

163. The RMF should be a central organisational feature of the investment firm, structured so that it can implement risk policies and control the risk management framework. The RMF should play a key role in ensuring that the investment firm has effective risk management processes in place. The RMF should be actively involved in all material risk management decisions.

164. In a group, the RMF in the Union parent undertaking should be able to deliver a group-wide holistic view on all risks and to ensure that the risk strategy is complied with.

165. The RMF should provide relevant independent information, analyses and expert judgement on risk exposures, and advice on proposals and risk decisions made by business lines or internal units, and should inform the management body as to whether such information and advice is consistent with the investment firm's risk strategy and risk appetite. The RMF may recommend improvements to the risk management framework and corrective measures to remedy breaches of risk policies, procedures and limits.

18.1 RMF's role in risk strategy and decisions

166. The RMF should be actively involved at an early stage in developing the investment firm's risk strategy and ensuring that the investment firm has effective risk management processes in place. The RMF should provide the management body with all relevant risk-related information to enable it to set the investment firm's risk appetite level. The RMF should assess the robustness and sustainability of the risk strategy and appetite. It should ensure that risk appetite is appropriately translated into specific risk limits. The RMF should also assess the risk strategies of business units, including targets proposed by the business units, and should be involved before a decision is made by the management body concerning the risk strategies and risk appetite. Targets should be plausible and consistent with the investment firm's risk strategy and risk appetite.

167. The RMF's involvement in decision-making processes should ensure that risk considerations are taken into account appropriately. However, accountability for the decisions taken should remain with the business and internal units, and ultimately the management body.

18.2 RMF's role in material changes

168. Before decisions on material changes to processes or systems or exceptional transactions are taken, the RMF should be involved in the evaluation of the impact of such changes and exceptional transactions on the investment firm's and group's overall risk, and should report its findings directly to the management body before a decision is taken.

169. The RMF should evaluate how the risks identified could affect the investment firm's or group's ability to manage its risk profile, liquidity and its sound capital base under normal and adverse circumstances.

18.3 RMF's role in identifying, measuring, assessing, managing, mitigating, monitoring and reporting on risks

170. The RMF should ensure that that there is an appropriate risk management framework and that all risks are identified, assessed, measured, monitored, managed and properly reported on by the relevant units in the investment firm.

171. The RMF should ensure that identification and assessment are not based only on quantitative information or model outputs, but also take into account qualitative approaches. The RMF should keep the management body informed of the assumptions used in, and the potential shortcomings of, the risk models and analysis.

172. The RMF should ensure that transactions with related parties are reviewed and that the risks they pose for the investment firm are identified and adequately assessed.

173. The RMF should ensure that all identified risks are effectively monitored by the business units.

174. The RMF should regularly monitor the actual risk profile of the investment firm and scrutinise it against the investment firm's strategic goals and risk appetite to enable decision-making by the management body in its management function and challenges by the management body in its supervisory function.

175. The RMF should analyse trends and recognise new or emerging risks and increases in risk arising from changing circumstances and conditions. It should also regularly review actual risk outcomes against previous estimates (i.e. back testing) to assess and improve the accuracy and effectiveness of the risk management process.

176. The RMF should evaluate possible ways to mitigate risks. Reporting to the management body should include proposals for appropriate risk-mitigating actions.

18.4 RMF's role in limits

177. The RMF should independently assess breaches of risk appetite or limits (including ascertaining the cause and undertaking a legal and economic analysis of the actual cost of closing, reducing or hedging the exposure against the potential cost of keeping it). The RMF should inform the business units concerned and the management body, and recommend possible remedies. The RMF should report directly to the management body in its supervisory function when the breach is material, without prejudice for the RMF to report to other internal functions and committees.

178. The RMF should play a key role in ensuring that a decision on its recommendation is made at the relevant level, complied with by the relevant business units and appropriately reported to the management body and, where established, the risk committee.

18.5 Head of the risk management function

179. Where established, the head of the RMF should be responsible for providing comprehensive and understandable information on risks and advising the management body, enabling this body to understand the investment firm's overall risk profile. The same applies to the head of the RMF of a parent investment firm regarding the consolidated situation. Where no independent function has been established, the responsibilities of the head of the risk management function lie with the staff to whom the risk management procedures are entrusted or the members of the management body directly.

180. The head of the RMF should have sufficient expertise, independence and seniority to challenge decisions that affect an investment firm's exposure to risks. Where the head of the RMF is not a member of the management body, taking into account the principle of proportionality as set out in Title I, investment firms should appoint an independent head of the RMF who has no responsibilities for other functions and reports directly to the management body. Where it is not proportionate to appoint a person who is dedicated only to the role of head of the RMF, taking into account the principle of proportionality as set out in Title I, this function can be

combined with the head of the compliance function or can be performed by another senior person, provided there is no conflict of interest between the tasks performed. In any case, this person should have sufficient authority, stature and independence (e.g. head of legal).

181. The head of the RMF should be able to challenge decisions taken by the investment firm's management and its management body, and the grounds for objections should be formally documented. If an investment firm wishes to grant the head of the RMF the right to veto decisions (e.g. a credit or investment decision or the setting of a limit) made at levels below the management body, it should specify the scope of such a veto right, the escalation or appeal procedures, and how the management body will be involved.

182. Investment firms should establish strengthened processes for the approval of decisions on which the head of the RMF has expressed a negative view. In its supervisory function, the management body should be able to communicate directly with the head of the RMF on key risk issues, including developments that may be inconsistent with the investment firm's risk strategy and risk appetite.

19 Compliance function[35]

183. Investment firms should establish a permanent and effective compliance function to manage compliance risk, and should appoint a person to be responsible for this function across the entire investment firm (the compliance officer). The compliance function, policies and procedures should also be compliant with Article 22 of Commission Delegated Regulation (EU) 2017/565 and ESMA guidelines on the compliance function.

184. The role of compliance officer, taking into account the principle of proportionality as set out in Title I, can be combined with the head of the RMF or, where it is not proportionate to appoint a person who is dedicated only to this function, can be performed by another senior person (e.g. head of legal), provided there is no conflict of interest between the tasks performed.

185. Staff within the compliance function should possess sufficient knowledge, skills and experience in relation to compliance and relevant procedures, and should have access to regular training.

186. The management body in its supervisory function should oversee the implementation of a well-documented compliance policy, which should be communicated to all staff. Investment firms should set up a process to regularly assess changes in the law and regulations applicable to its activities.

187. The compliance function should advise the management body on measures to be taken to ensure compliance with applicable laws, rules, regulations and standards, and should assess

[35] This section should be read without prejudice and in conjunction with the ESMA guidelines on the compliance function.

the possible impact of any changes in the legal or regulatory environment on the investment firm's activities and compliance framework.

188. The compliance function should ensure that compliance monitoring is carried out through a structured and well-defined compliance monitoring programme and that the compliance policy is observed. The compliance function should report to the management body and communicate as appropriate with the RMF on the investment firm's compliance risk and its management. The compliance function and the RMF should cooperate and exchange information as appropriate to perform their respective tasks. The findings of the compliance function should be taken into account by the management body and the RMF in decision-making processes.

189. Investment firms should take appropriate action against internal or external behaviour that could facilitate or enable fraud, ML/TF or other financial crime and breaches of discipline (e.g. breaches of internal procedures or breaches of limits).

190. Investment firms should ensure that their subsidiaries and branches take steps to ensure that their operations are compliant with local laws and regulations. If local laws and regulations hamper the application of stricter procedures and compliance systems implemented by the group, especially if they prevent the disclosure and exchange of necessary information between entities within the group, subsidiaries and branches should inform the compliance officer or the head of compliance of the Union parent undertaking.

20 Internal audit function

191. Where established, the IAF should be independent and have sufficient authority, stature and resources. In particular, investment firms should ensure that the qualification of the IAF's staff members and the IAF's resources, in particular its auditing tools and risk analysis methods, are adequate for the investment firm's size and locations, and the nature, scale and complexity of the risks associated with the investment firm's business model, activities, risk culture and risk appetite.

192. The IAF should be independent of the audited activities. Therefore, the IAF should not be combined with other functions.

193. The IAF should, following a risk-based approach, independently review and provide objective assurance of the compliance of all activities and units of an investment firm, including outsourced activities, with the investment firm's policies and procedures and with external regulatory requirements. Each entity within the group should fall within the scope of the IAF.

194. The IAF should not be involved in designing, selecting, establishing or implementing specific internal control policies, mechanisms, procedures or risk limits. However, this should not prevent the management body in its management function from requesting input from internal audit on matters relating to risk, internal controls and compliance with applicable rules.

195. The IAF should assess whether the investment firm's internal control framework as set out in Section 15 is both effective and efficient. In particular, the IAF should assess:

    a. the appropriateness of the investment firm's governance framework;

    b. whether existing policies and procedures remain adequate and comply with legal and regulatory requirements and with the risk strategy and risk appetite of the investment firm;

    c. the compliance of the procedures with the applicable laws and regulations and with decisions of the management body;

    d. whether the procedures are correctly and effectively implemented (e.g. compliance of transactions, the level of risk effectively incurred, etc.); and

    e. the adequacy, quality and effectiveness of the controls carried out and the reporting conducted by the business units (first line of defence) and the risk management and compliance functions.

196. The IAF should verify, in particular, the integrity of the processes ensuring the reliability of the investment firm's methods and techniques, and the assumptions and sources of information used in its internal models (e.g. risk modelling and accounting measurements). It should also evaluate the quality and use of qualitative risk identification and assessment tools and the risk mitigation measures taken.

197. The IAF should have unfettered investment firm-wide access to all the records, documents, information and buildings of the investment firms. This should include access to management information systems and minutes of all committees and decision-making bodies.

198. The IAF should adhere to national and international professional standards. An example of the professional standards referred to here is the standards established by the Institute of Internal Auditors.

199. Internal audit work should be performed in accordance with an audit plan and a detailed audit programme following a risk-based approach.

200. An internal audit plan should be drawn up at least once a year on the basis of the annual internal audit control objectives. The internal audit plan should be approved by the management body.

201. All audit recommendations should be subject to a formal follow-up procedure by the appropriate levels of management to ensure and report on their effective and timely resolution.

Title VI – business continuity management

202. Investment firms should establish a sound business continuity management and recovery plan to ensure their ability to operate on an ongoing basis and to limit losses in the event of severe business disruption.

203. Investment firms may establish a specific independent business continuity function.

204. An investment firm's business relies on several critical resources (e.g. IT systems, including cloud services, communication systems, core staff and buildings). The purpose of business continuity management is to reduce the operational, financial, legal, reputational and other material consequences arising from a disaster or extended interruption to these resources and consequent disruption to the investment firm's ordinary business procedures. Other risk management measures might be intended to reduce the probability of such incidents or to transfer their financial impact to third parties (e.g. through insurance).

205. In order to establish a sound business continuity management plan, an investment firm should carefully analyse risk factors for, and its exposure to, severe business disruptions and assess (quantitatively and qualitatively) their potential impact, using internal and/or external data and scenario analysis. This analysis should cover all business lines and internal units, including the RMF or risk management procedures, and should take into account their interdependency. The results of the analysis should contribute to defining the investment firm's recovery priorities and objectives.

206. On the basis of the abovementioned analysis, an investment firm should put in place:

    a. contingency and business continuity plans to ensure that the investment firm reacts appropriately to emergencies and is able to maintain its most important business activities if there is disruption to its ordinary business procedures; and

    b. recovery plans for critical resources to enable the investment firm to return to ordinary business procedures in an appropriate timeframe. Any residual risk from potential business disruptions should be consistent with the investment firm's risk appetite.

207. Contingency, business continuity and recovery plans should be documented and carefully implemented. The documentation should be available within the business lines, internal units and RMF for staff in charge of risk management procedures, and should be stored on systems that are physically separated and readily accessible in case of contingency. Appropriate training should be provided. Plans should be regularly tested and updated. Any challenges or failures occurring in the tests should be documented and analysed, with the plans reviewed accordingly.

Title VII – transparency

208. Strategies, policies and procedures should be communicated to all relevant staff throughout an investment firm. An investment firm's staff should understand and adhere to policies and procedures pertaining to their duties and responsibilities.

209. Accordingly, the management body should inform and update the relevant staff about the investment firm's strategies and policies in a clear and consistent way, at least to the level needed to carry out their particular duties. This may be done through written guidelines, manuals or other means.

210. Where parent undertakings are required by competent authorities under Article 44 of Directive (EU) 2019/2034 to publish annually a description of their legal structure and governance and the organisational structure of the group of investment firms, the information should include all entities within the group structure as defined in Directive (EU) 2013/34[36], by country.

211. The publication should include at least:

    a. an overview of the internal organisation of the investment firm and the group structure as defined in Directive (EU) 2013/34 and changes thereto, including the main reporting lines and responsibilities;

    b. any material changes since the previous publication and the date of the material change;

    c. new legal, governance or organisational structures;

    d. information on the structure, organisation and members of the management body, including the number of its members and the number of those qualified as independent, and specifying the gender and duration of the mandate of each member of the management body;

    e. the key responsibilities of the management body;

    f. a list of the committees of the management body in its supervisory function and their composition;

    g. an overview of the conflicts of interest policy applicable to the investment firm and to the management body;

    h. an overview of the internal control framework; and

[36] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC (OJ L 182, 29.6.2013, p. 19)

i. an overview of the business continuity management framework.

Annex I – aspects to take into account when developing an internal governance policy

In line with Title III, investment firms should consider the following aspects when documenting internal governance policies and arrangements:

1. Shareholder structure
2. Group structure, if applicable (legal and functional structure)
3. Composition and functioning of the management body
    a) selection criteria including how diversity is taken into account
    b) number, length of mandate, rotation, age
    c) independent members of the management body
    d) executive members of the management body
    e) non-executive members of the management body
    f) internal division of tasks, if applicable
4. Governance structure and organisation chart (with impact on the group, if applicable)
    a) specialised committees
        i. composition
        ii. functioning
    b) executive committee, if any
        i. composition
        ii. functioning
5. Key function holders
    a) head of the risk management function
    b) head of the compliance function
    c) head of the internal audit function
    d) chief financial officer
    e) other key function holders
6. Internal control framework
    a) description of each function, including its organisation, resources, stature and authority
7. Description of the risk strategy and risk management framework

8. Organisational structure (with impact on the group, if applicable)
    a) operational structure, business lines, and allocation of competences and responsibilities
    b) outsourcing
    c) range of products and services
    d) geographical scope of business
    e) provision of services under the regime of freedom of provision of services
    f) branches
    g) subsidiaries, joint ventures, etc.
    h) use of offshore centres
9. Code of conduct and behaviour (with impact on the group, if applicable)
    a) strategic objectives and company values
    b) internal codes and regulations, including anti money laundering and counter terrorism financing policies
    c) conflict of interest policy
    d) whistleblowing
10. Status of the internal governance policy, with date
    a) development
    b) last amendment
    c) last assessment
    d) approval by the management body.

5. Accompanying documents

5.1. Cost-benefit analysis/impact assessment

1. Article 16(2) of Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority) (EBA Regulation) provides that the EBA should carry out an analysis of 'the potential related costs and benefits' of any guidelines it develops. This analysis should provide an overview of the findings regarding the problem to be dealt with, the solutions proposed and the potential impact of these options.

A. Problem identification and policy objectives

2. Directive (EU) 2019/2034 is setting out specific requirements on internal governance arrangements for investment firms that are not small and not interconnected. The EBA has been mandated under Article 26 Directive (EU) 2019/2034 to issue guidelines, in consultation with ESMA, on the application of the governance arrangements referred to in paragraph 1 of this Article.

B. Baseline scenario

3. The current EU legislative framework for investment firms' governance arrangements mainly consists of Directive 2013/36/EU, Directive 2014/65/EU, the Commission Delegated Regulation (EU) 2017/565 and the Commission Delegated Directive (EU) No 2017/593, the EBA guidelines on sound remuneration policies, the joint EBA and ESMA guidelines on the assessment of the suitability of members of the management body and key function holders, the ESMA guidelines on certain aspects of the MiFID II compliance function requirements, the ESMA guidelines on product governance and the ITS guidelines on disclosures.

4. The impact assessment covers guidelines developed to ensure the harmonised application of investment firms' governance requirements introduced by Directive (EU) 2019/2034 where they differ from the previously applicable framework and from the MiFID framework. Areas that have not changed in substance and the changes introduced within the Directive (EU) 2019/2034 (IFD) and Regulation (EU) 2019/2033 have not been assessed.

C. Options considered

Implementation date

5. Specific governance requirements are being introduced for investment firms by implementing Directive (EU) 2019/2034 into national law on 26 June 2021.

6. Considering that the IFD governance framework as such is equivalent to the requirements under the CRD, a short implementation period is sufficient. However, some of the requirements under the IFD require some limited changes to investment firms' internal governance arrangements and documentation. This concerns e.g. the establishment of a risk committee and a remuneration committee for investment firms whose value of on and off-balance sheet assets is on average more than EUR 100 million over the four-year period immediately preceding the given financial year, but also the diversity aspect and the conflicts of interest policy regarding related-party transactions. A few investment firms have previously not been subject to the CRD requirements. Hence, an application date of the guidelines that specify these requirements in detail of 30 April 2022 appears appropriate.

Risk committee

7. The IFD requires investment firms that have on and off-balance sheet assets of on average more than EUR 100 million over the four-year period immediately preceding the given financial year to establish a risk committee. Guidance has been provided on the composition and tasks of this committee.

8. Option A: the guidelines should follow exactly the same approach regarding the composition of this committee as for CRD institutions to ensure a consistent approach among sectors.

9. Option B: the guidelines should follow a more proportionate approach, taking into account the nature and complexities of investment firms' activities. Where the number of members within the management body in its supervisory function is insufficient to ensure a sound composition of committees as set out in this section, the tasks of the committee may be delegated to one member of the management body in its supervisory function, who is supported as appropriate by staff. Committees may be composed of the same group of members, taking into account the criteria set out in Title I and the number of independent members of the management body in its supervisory function and the specific experience, knowledge and skills that are individually or collectively required for the committees. The reasoning for the composition of committees should be documented.

   Option A would lead to some additional costs for investment firms compared to Option B. Option B follows a more proportionate approach to setting up committees.

   Option B has been retained.

Loans and other transactions with members of the management body and their related parties

10. Related party transactions are a specific source of actual or potential conflicts of interest, and specific guidance has been developed for the prudent management of conflicts of

interest that might be created by such transactions and to ensure that firms have appropriate decision management and oversight processes for such transactions.

11. Option A: replicate the same approach taken under the CRD, adapting it to investment firms' business models and with a more proportionate approach taken into account. Indeed, investment firms do not usually grant loans other than in specific cases.

12. Option B: not providing guidelines on related party transactions

    Regarding option A, the objective of the changes is to ensure that there is sufficient scrutiny in respect of decisions regarding such loans when they are granted and other transactions and that conflicts of interest in this context are managed appropriately. Not providing guidance on this aspect would not be effective and would not ensure that investment firms have sound governance arrangements in line with the IFD and MiFID. Documentation of loans is required to monitor the relevant practices.. In this case, investment firms should document loans with their management body and their related party. Minor additional costs are created, caused by specific additional documentation requirements that are necessary to ensure that the impact of such loans and the conflicts of interest they potentially create can be assessed by firms and competent authorities. However the level of detail has been reduced to take into account the fact that investment firms do not usually grant loans. In line with the principle of proportionality, the guidelines differentiate between requirements for material and non-material loans.

Option A was retained

Diversity and gender-neutral pay

13. The guidelines aim to further specify requirements under the IFD and to achieve harmonisation at the EU level. Given the need for Member States to implement the IFD provisions and to abide by the principles set out within the European Charter of Fundamental Rights, it is presumed that the guidelines do not lead to any conflicts regarding these matters. Investment firms' policies must be gender-neutral. Some aspects concerning equal opportunities and anti-discrimination have been further specified in the guidelines. In the same way as for CRD institutions, investment firms are required to document and monitor the trend in the gender pay gap.

14. Option A: replicate the same approach taken under the CRD.

15. Option B: adapting it to investment firms' business models and with a more proportionate approach. Indeed, monitoring the trend in the gender pay gap could be required only where investment firms have 50 or more staff in accordance with the threshold foreseen under the Commission recommendation of 7 March 2014 on strengthening the principle of equal pay between men and women through transparency.

Option A would lead to some additional burdens for investment firms compared to option B.

Option B was retained.

Internal control framework and the three lines of defence.

16. Option A: requiring Class 2 firms to set up three independent functions (compliance, risk management and internal audit functions)

17. Option B: establishing a more proportionate approach, also to be consistent with the MiFID framework; a permanent and effective compliance function should be set up; firms are not required to set up an internal risk management function, where justified. However, firms should implement policies and process to achieve the same objectives and should have a sound and effective internal control framework.

18. Option A is not recommended, as it does not lead to greater sectoral consistencies. It would cause additional costs to establish a sound internal control framework and ensure the independence of the internal control functions.

19. Option B is recommended to create consistency between the MiFID and CRD frameworks. By implementing policies and processes to achieve the same objectives, firms would still benefit from an effective framework, which would lead to a better alignment of the risk profile with risk appetite as set by the management body.

Option B was retained.

E. Cost-benefit analysis

20. Given the limited changes compared to the baseline scenario and the easing of some requirements within the IFD, and given that most of the governance arrangements already exist under the MiFID framework, it is assumed that the changes to the guidelines create low implementation costs, mainly for updates to internal policies and the additional documentation required.

5.2. Feedback on the public consultation and opinion of the Banking Stakeholder Group

Summary of key issues and the EBA's response

The EBA published its consultation paper on 17 December 2020 and received 10 responses in total. Eight of them were published, while one was submitted on a confidential basis. The Banking Stakeholder Group did not submit its views. The last response was submitted too late and will therefore not be published. The consultation concerned the whole draft guidelines on internal governance under the IFD, which complete the various governance provisions in Directive (EU) 2019/2034.

The main comments received challenged the fact that the draft guidelines are based on the current guidelines on internal governance, which – according to the respondents – is not in line with the intention of the IFD, which establishes a simplified and proportionate regime for investment firms. The respondents consider the draft guidelines to be too extensive for investment firms covered by them.

In addition, some respondents believed that the draft guidelines do not take into account the internal governance requirements set out under MiFID II and the Commission Delegated Regulation (EU) 2017/565, which in particular include specific provisions regarding internal control functions, whistleblowing schemes and conflicts of interest policies. They point out that dual regulation in this area is unjustified, unnecessary, and burdensome to investment firms.

A detailed analyses of the comments received is included in the feedback table below.

Summary of responses to the consultation and the EBA's analysis

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
General comments			
Guidelines on internal governance under the CRD	Several respondents comment that the draft GL are very similar to those currently in effect and applicable to CRD and MiFID firms. As the intention of the IFD is to put in place a prudential framework that is more appropriate for investment firms, the respondents urged the EBA to take a similar approach in considering the appropriate governance requirement for investment firms. The draft GL is too extensive for non-systemically important investment firms. They also feel that the GLs overlap with MiFID II and the Commission Delegated Regulation (EU) 2017/565 and suggest deleting all the requirements that are not covered by Article 26 IFD but are subject to MiFID II. One respondent is concerned that the concept of significant firms used in the CRR has been incorporated into the GL in relation to firms	Guidelines are in line with the mandate provided under Article 26 of the IFD and are consistent with the MiFID framework, including with Commission Delegated Regulation (EU) 2017/565. A careful assessment was made in cooperation with the ESMA. In accordance with the proportionality principle, the guidelines take into account the specificities of investment firms. Significant investment firms (class 1) are subject to the CRD/CRR framework. Investment firms for which the value of their on and off-balance sheet assets is on average more than EUR 100 million over the four-year period immediately preceding the given financial year must establish risk and remuneration committees to advise the management body in its supervisory function and to prepare the decisions to be taken by this	No change

	with a balance sheet above EUR 100m. It is disproportionate to carry over the provisions – this applies only to significant CRR firms – to all IFD firms with a balance sheet above EUR 100m.	body. This is fully in line with Article 28 of the IFD. Another threshold can be specified by national law. Finally, it should be stressed that the guidelines on internal governance under the IFD do not apply to small and non-interconnected investment firms (class 3 firms).	
Scope of the guidelines on internal governance under the CRD	One respondent disagrees with the EBA's assessment that the CRD governance requirements already apply to all investment firms covered by the IFD governance rules. The definition of investment firms in the CRD/CRR does not encompass entities providing certain MiFID services without a licence to hold client money or to deal on their own account. For such limited licence firms that do not meet the thresholds in Article 12 IFR, the IFD framework lays down new governance requirements in addition to the MiFID.	Under CRD IV, a set of investments were already subject to governance requirements and were therefore included in this framework. Under CRD V, only class 2 firms are subject to governance requirements. It should be stressed, however, that all investment firms are subject to governance requirements under MIFID.	No change
Para. 24 Background	One respondent suggests clarifying that small and non-interconnected investment firms are not required to set up governance rules regarding liquidity risks on an intra-day basis as a standard process.	In accordance with Article 29 (3), competent authorities should ensure that small and non-interconnected investment firms have robust strategies, policies, processes and systems for the identification, measurement, management and monitoring of liquidity risk over an	No change

		appropriate set of time horizons, including intra-day, so as to ensure that the investment firm maintains adequate levels of liquid resources.	
Responses to questions in Consultation Paper EBA/CP/2020/27			
Q1. Are the subject matter, scope of application, definitions and date of application appropriate and sufficiently clear?			
Para. 1 Status of these guidelines	One respondent suggests replacing the term 'financial institutions, including investment firms' with the term 'investment firms covered by Article 26 of the Directive (EU) 2019/2034'.	The use of this wording is in line with the EBA's foundation as referred to in Article 4 (1) of Regulation (EU) No 1093/2010 and explicitly refers to investment firms as defined in Article 4(1)(1) of Directive 2014/65/EU.	No change
Para. 5 Subject matter	One respondent suggests clarifying the subject matter so that *'Section 2 of Chapter 2'* is amended to *'Article 26'.*	Section 2 of Chapter 2 refers to internal governance, transparency, treatment of risks and remuneration, so it is sufficiently clear. Article 26 refers only to a single provision.	No change
Para. 7 Addressees	One respondent suggests amending the addressees of the guidelines so that the scope of the guidelines is clearly limited to investment firms within the meaning of Article 2 IFD that are authorised and supervised under MiFID II, instead of financial institutions as referred to in	In accordance with Article 2 the IFD applies to investment firms authorised and supervised under Directive 2014/65/EU. In addition, the guidelines specify further that the governance requirements do not apply to small and non-interconnected investment firms (class 3 firms)	No change

	Article 4 (1) of Regulation (EU) No 1093/2010, which are investment firms as defined in Article 4(1)(1) of MiFID II.	as referred to under Article 12(1) of Regulation (EU) 2019/2033.	
Para. 8-14 Scope of application	One respondent suggests clarifying that the governance rules also cover the activities of investment firms providing portfolio management without a licence for dealing on their own account or holding client assets or money in an appropriate and proportionate way. The draft guidelines (in particular the requirements on the tasks and responsibilities of the risk management function) are only focused on the investment firms' risk profile.	In accordance with the IFD, the guidelines on internal governance apply to all investment firms that do not qualify as small and non-interconnected investment firms (class 3 firms) as referred to under Article 12(1) of Regulation (EU) 2019/2033. They also apply in a proportionate manner, and a section further specifies how to take into account the application of the proportionality principle.	No change
Para. 16 Date of application	Several respondents suggest postponing the date of application by at least 6 months.	The comment has been taken into account. The guidelines will enter into force on 30 April 2022. However, this does not change the fact that investment firms have to comply with the national implementation of the IFD when it comes into force.	Guidelines amended
Q2. Is Title II+(I) sufficiently clear? Do you think other criteria should be added or deleted as inappropriate?			
Title I – proportionality			

Para. 20 Proportionality	Several respondents comment that the description of proportionality is too complex and extensive since the criteria are difficult to assess in practice. This results in different assessments, which causes competitive disadvantages for some companies. In addition, a few respondents request clarification that in assessing what is proportionate, the focus should be on the combination of all the criteria mentioned since the amount of assets under management are not suitable or eligible to be a standalone criterion in order to ensure an appropriate implementation of the governance requirements. Some respondents suggest that institutions could be given the discretion to define the specific arrangements for the individual requirements – depending on the risk and complexity of their business model and risk profile.	The governance arrangements should be appropriate and proportionate to the nature, scale and complexity of the risks inherent in the business model and the activities of the investment firm. This section further specifies how to take into account criteria for the application of the proportionality principle. This is not an exhaustive list, and an investment firm may also consider a combination of these criteria. When applying these criteria, investment firms should also be able to demonstrate to their CA that they are relevant to their businesses. The criteria listed further specify the principle of proportionality, are non-exhaustive and fully relevant to investment firms.	No change
Title II – role and composition of the management body			
Management body	One respondent suggests that the competences of the management body should be aligned with MiFID II.	The competence of the management body is consistent with the MiFID framework and in line with the IFD mandate under article 26.	No change

Para. 22-31 Role and responsibilities of the management body	One respondent suggests that employee/trade union representation is given a place on the management body in countries and companies where such representation is present.	The management body includes representatives of employees where applicable. There is no need to specify this point. This section is about the management body as a collegiate body.	No change
Para. 26 Role and responsibilities of the management body	One respondent requests clarifying that a 'suitable business model' does not mean an ESG business model with the requirement to ensure strategies are based on sustainable finance models.	The paragraph has been clarified.	Guidelines amended
Section 3 Supervisory function of the management body	One respondent suggests clarifying how investment firms should consider the application of these requirements, in particular para. 37 and 38 where the EBA suggests that national law would take precedence over EBA guidelines. One respondent asks for further clarification about the reference to section 9.3 of the joint ESMA and EBA guidelines on suitability as a reference to the independence criteria in paragraph 91 or to the categories of firms that are required to have independent directors in	The guidelines specify that the terms 'management body in its management function' and 'management body in its supervisory function' are used throughout these guidelines without referring to any specific governance structure, and references to the management (executive) or supervisory (non-executive) function should be understood as applying to the bodies or members of the management body responsible for that function in accordance with national law. When implementing these guidelines, competent authorities should take into	No change

	paragraph 89. If the former, paragraph 37 exceeds the requirements of the level 1 text. If the latter, the guidelines should make it clear the reference made to the scope of application of the requirement to have independent directors and that the references therein to CRD firms do not provide sufficient clarity once investment firms become subject to the IFD. This is not supported by the level 1 text in terms of requirements to have independent directors.	account their national company law and specify, where necessary, to which body or members of the management body these functions should apply. Please refer to the EBA and ESMA guidelines on suitability. Under the updated joint EBA and ESMA guidelines on suitability, investment firms as defined in Article 4(1)(1) of Directive 2014/65/EU that do not meet all of the conditions for qualifying as small and non-interconnected investment firms under Article 12(1) of Regulation (EU) 2019/2033 and that are neither significant nor listed should, as a general principle, have at least one independent member on the management body in its supervisory function. However, competent authorities may not require any independent directors under specific conditions foreseen in the guidelines.	
Section 5 Committees of the management body	One respondent notes that the requirement to have separate governance committees conflicts with the proportionality objective of the IFD and asks that the guidelines are amended to enable firms that are treated as significant	In accordance with Article 28 of the IFD and unless otherwise specified by national law[37], investment firms for which the value of on and off-balance sheet assets is on average more than EUR 100 million over the four-year period	No change

[37] Article 28 of Directive (EU) 2019/2034 requires that Investment firms that do not meet the criteria set out in point (a) of Article 32(4) to establish a risk committee composed of members of the management body who do not perform any executive function in the investment firm concerned.

in its supervisory function	under IFD/IFR to implement proportionate structures.	immediately preceding the given financial year must establish risk and remuneration [38] committees to advise the management body in its supervisory function and to prepare the decisions to be taken by this body.	
Para. 49, 51 and 53 Composition of committees	One respondent suggests revising the provisions, which are not supported by the IFD, which includes no requirements for independent directors. This requirement is disproportionate in the light of CRD V requirements, which would have exempted non-significant CRD investment firms from the requirement generally.	The EBA must issue specific guidelines whenever explicitly required under European Union law. This is the case for Article 26, which mandates the EBA and ESMA to issue guidelines on governance arrangements, processes and internal control mechanisms. In addition, Article 16 of EBA Regulation (EU) No 1093/2010 lays down the general competence to issue guidelines ensuring the common, uniform and consistent application of Union within its scope of action law and effective supervisory practices within the ESFS. The same holds true for the ESMA. Accordingly, the guidelines do not go beyond the scope of their mandate. Independence is part of sound governance arrangements.	No change
Q3. Is Title III sufficiently clear and appropriate?			

[38] With regard to the remuneration committee, please refer to the EBA guidelines on sound remuneration practices under Directive (EU) 2019/2034.

Definitions of parent investment firms and their subsidiaries	One respondent requests reviewing all references to 'parent investment firms and their subsidiaries' and all other terms and definitions used in the group context. The terms used do not comply with the definitions and scope of the prudential consolidation of the IFD/IFR framework in all cases. Not every parent company of an investment firm group is an investment firm. This applies, in particular, to the general group approach in paragraph 77. The respondent disagrees with the scope definition stating that the 'parent investment firms and their subsidiaries' should ensure that governance arrangements are consistent and well-integrated on a consolidated basis.	The guidelines have been clarified and consistent terminology has been used for 'EU parent undertakings'. The group application section is fully in line with the IFD, which refers to the CRD/CRR framework in respect of this matter. Within a group context, the EU parent undertakings should ensure that governance arrangements are coherent and consistent within the group.	No change
Para. 83 Organisational framework in a group context	One respondent suggests clarifying how 'these guidelines apply irrespective of the fact that they may be subsidiaries of a parent investment firm in a third country'. The statement seems to be in conflict with the sentiment conveyed in para. 37 and 38 of the GL.	The guidelines apply to investment firms located in the EU irrespective of the fact that they may be subsidiaries of a parent investment firm in a third country. The guidelines have been clarified.	Guidelines amended
Q4. It Title IV appropriate and sufficiently clear? In particular the item on conflicts of interest and RPT at investment firms. Should we keep it like this?			

Para. 92 Corporate values and code of conduct	One respondent proposes adding that the proportionality principle should be considered when it comes to gender equality in management positions.	The guidelines have been clarified. Investment firms' policies should be gender-neutral.	Guidelines amended
Para. 10 Conflicts of interest policy at firm level	One respondent suggests clarifying whether investment firms are expected to establish a conflicts of interest policy in addition to the one that already exists within investment firms in order to comply with MiFID II and regulation 2017/565. Several respondents suggest deleting this part.	A separate policy is not required. However, the conflicts of interest policy should be in line and consistent with the framework under MiFID II and the Commission Delegated Regulation (EU) 2017/565 and also the IFD, as further specified in these guidelines.	No change
Para. 123 Internal alert procedures	One respondent suggests strengthening this paragraph by adding that the whistleblower's identity should be kept confidential and preferably anonymous for as long as possible.	In accordance with the IFD, the guidelines specify that where required by the staff member reporting a breach, the information should be provided to the management body and other responsible functions in an anonymised way. Investment firms may also establish a whistleblowing process that allows information to be submitted in an anonymised way.	No change
Para. 126(d)	One respondent would like clarification regarding this reference.	The guidelines have been clarified.	Guidelines amended

Reporting breaches to competent authorities			
Q5. Is Title V appropriate and sufficiently clear?			
Section 18-21 Internal control functions	A few respondents suggest excluding section 18-21 from the guidelines since MiFID II and Regulation (EU) 2017/565 include appropriate provisions on this matter. In addition, the ESMA has developed guidelines regarding the compliance function.	Consistency has been ensured with ESMA products.	No change
Para. 193 Internal audit function	One respondent would like clarification with regard to this reference.	The guidelines have been clarified.	Guidelines clarified
Q6. Is Title VI appropriate and sufficiently clear?			
Para. 200-205	One respondent suggests reviewing the provisions relating to the internal risk management requirements of supervised entities regarding ICT risks and activities since	The EBA will issue further guidance in line with the mandates received in the upcoming Directive.	No change

	this will be specified in the new Regulation (DORA).		
Business continuity management	One respondent suggests clarifying what is meant by ‘appropriate’ in terms of how often this training is provided and under what framework.	The appropriate frequency depends on the criticality of the process or system and staff awareness of such procedures.	No change

ANNEX 3: EBA GUIDELINES ON SOUND REMUNERATION POLICIES FOR INVESTMENT FIRMS (EBA/GL/2021/13)

EBA/GL/2021/13

22 November 2021

Final Report

on Guidelines on sound remuneration policies under Directive (EU) 2019/2034

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Executive Summary

Investment firms have to apply sound remuneration policies to all staff and some specific requirements for the variable remuneration of staff whose professional activities have a material impact on the risk profile of the investment firms or the assets they manage (identified staff) under Directive (EU) 2019/2034 (IFD)). The IFD mandates the EBA to develop guidelines on remuneration policies for all staff as part of investment firm's internal governance arrangements, remuneration policies for identified staff that take into account the criteria in Articles 30 and 32 of the IFD and guidelines that facilitate the implementation of waivers by Member States.

The EBA published guidelines on remuneration policies under Directive 2013/36/EU (CRD) in 2015 that were applicable to credit institutions and investment firms. Those guidelines form the basis for the present guidelines, as the underlying provisions in CRD and IFD follow the same regulatory approach. In addition, the requirements for investment firms, introduced by the IFD, are further specified in these guidelines. The alignment of the frameworks for credit institutions and investment firms ensures a level playing field and cross-sectoral consistency, while the application of the principle of proportionality is taken into account.

The guidelines are addressed to investment firms as defined in Article 4(1)(1) of Directive 2014/65/EU that do not meet all of the conditions for qualifying as small and non-interconnected investment firms under Article 12(1) of Regulation (EU) 2019/2033 and competent authorities. The guidelines apply on an individual basis in accordance with Article 25 IFD and Article 7 of Regulation 2019/2033/EU (IFR) and unless Article 8 of the IFR is applied by competent authorities, on a consolidated basis. All investment firms must also comply with the national implementation of requirements under Directive 2014/65/EU (MiFID).

The guidelines specify further the requirements on remuneration policies in Directive (EU) 2019/2034 with regard to the respective governance arrangements and processes which should be applied when remuneration policies for all staff and for identified staff are implemented. Remuneration policies must be gender neutral in accordance with Directive 2019/34/EU and respect the principle of equal pay for male and female workers for equal work or work of equal value. The guidelines specify the elements that investment firms should implement in this regard.

While parts of the guidelines concern sound and gender neutral remuneration policies for all staff, the main part of the guidelines focuses on the specific provisions that apply to investment firms' remuneration policies for identified staff. In particular for identified staff, the alignment of the variable remuneration with the risk profile of the investment firms or the assets they manage is crucial.

The guidelines will be applicable as of 30 April 2022.

Background and rationale

1. Inappropriate remuneration structures have been a contributing factor to excessive and imprudent risk taking. Poorly designed remuneration policies have potentially detrimental effects on the sound management of risks, control of risk and the risk taking behaviour of individuals. Most investment firms were subject to the remuneration framework under Directive 2013/36/EU (CRD) until 26 June 2021. Since then a specific prudential framework for investment firms set by Directive (EU) 2019/2034 (IFD) has applied. A few investment firms will continue to be subject to the CRD and will have to apply for authorisation as a credit institution. Some investment firms, that have not been subject to the CRD, are subject to specific requirements on remuneration policies for the first time. The guidelines foster a consistent application of the remuneration framework set out under Articles 30 to 33 IFD.

2. To a large extent, both frameworks (CRD and IFD) are equivalent, regarding the prudential remuneration requirements that will apply to investment firms (class 2 investment firms), unless they are small and not interconnected. The main differences are that for investment firms, no specific limitation of the ratio between variable and fixed remuneration is foreseen in the directive and that they have more flexibility regarding the instruments they can use for the award of variable remuneration to identified staff. All investment firms are also subject to remuneration requirements under Directive 2014/65/EU (MiFID) that aim to ensure responsible business conduct, fair treatment of clients and the appropriate management of conflicts of interest when conducting business.

3. The remuneration requirements aim to ensure that remuneration policies are consistent with and promote sound and effective risk management, do not provide for incentives for excessive risk taking, and are aligned with the long-term interests of the investment firms across the EU.

4. To ensure a more proportionate approach, the co-legislator introduced in Article 32(4) IFD the possibility to waive the requirement that a part of the variable remuneration of identified staff is paid out in instruments and is deferred. When applied to smaller investment firms, those requirements would be too burdensome and the cost would not be commensurate with the prudential benefits. This would also be the case for staff with low levels of variable remuneration, even if they are employed by larger investment firms. While those waivers are based on thresholds provided by the IFD, Member States have some discretion regarding their implementation. The EBA has a mandate to issue guidelines under Article 32(9) IFD to facilitate the implementation of waivers.

5. The IFD reinforces the principle of equal pay for male and female workers for equal work or work of equal value which is laid down in Article 157 of the Treaty on the Functioning of the European Union (TFEU). Investment firms should operate a gender neutral remuneration policy. In

accordance with Art 26 (4) IFD, the EBA shall issue guidelines, in accordance with Article 16 of Regulation (EU) No 1093/2010, on gender neutral remuneration policies for investment firms.

Legal basis

6. The guidelines are based on Article 16 of EBA founding Regulation 1093/2010, Articles 26, 32 and 34 of the IFD. These guidelines further specify the IFD remuneration requirements. Investment firms are subject to those requirements and the guidelines, unless the investment firm determines on the basis of Article 12(1) of Regulation (EU) 2019/2033 (IFR) that it meets all conditions for qualifying as small and non–interconnected investment firms. Investment firms that are subject to Title VII of Directive 2013/36/EU in application of Article 1(2) and (5) of the IFR are not subject to these guidelines but are subject to the EBA guidelines on sound remuneration policies under CRD. The guidelines apply on the individual and consolidated basis.

7. Article 26 of the IFD requires that investment firms have robust governance arrangements, including remuneration policies and practices that are gender neutral and that are consistent with and promote sound and effective risk management. The EBA has been mandated to issue guidelines, in accordance with Article 16 of Regulation (EU) No 1093/2010, on those arrangements, processes and mechanisms and to issue guidelines on gender neutral remuneration policies.

8. Furthermore, the EBA has been mandated to issue a report on the application of gender neutral remuneration policies by investment firms within two years of the date of publication of the guidelines on gender neutral remuneration policies.

9. Article 32(9) mandates the EBA to adopt guidelines that facilitate the implementation of the waivers encoded in paragraphs 4, 5 and 6 of this Article. Article 34(3) of the IFD mandates the EBA to develop guidelines with respect to remuneration requirements contained in Articles 30 to 33 of the IFD. All those guidelines have been developed in close cooperation with ESMA.

10. These guidelines take due account of existing remuneration guidelines pursuant to Directives 2009/65/EC, 2011/61/EU and 2014/65/EU. Investment firms also need to comply with the requirements under Directive 2014/65/EU (MiFID) and the respective ESMA Guidelines. The guidelines should also be read in conjunction with other relevant EBA guidelines, in particular guidelines concerning the internal governance for investment firms and Delegated Regulatory Regulations mandated under Articles 30 (4) and 32(8) of the IFD on the identification of staff and on other instruments and alternative arrangements for the pay-out of variable remuneration.

Rationale and objective of the guidelines

11. In line with Article 16 of the EBA founding regulation 1093/2010, as amended, the guidelines aim to ensure that a level playing field is preserved amongst investment firms within Member States, taking into account the nature, scale and complexity of their activities. The guidelines complete the relevant provisions of the IFD and IFR in order to ensure that investment firms

implement sound remuneration policies which are based on sound governance processes, take into account the investment firms' risk strategy and profile, and align the incentives of staff with the interest of owners and other stakeholders.

12. To this end, guidance is given for both investment firms and competent authorities to ensure that a risk-aligned remuneration culture and framework in the financial sector is implemented, maintained and further developed in line with the regulatory requirements. In line with the above-mentioned objectives, the guidelines specify the requirements included in the IFD on remuneration policies for all staff and the specific provisions on remuneration policies for staff whose professional activities have a material impact on the investment firms' risk profile or of the assets that it manages (identified staff) and their implementation.

13. The guidelines differentiate between the provisions applicable to all staff and provisions applicable to identified staff. As identified staff have a higher impact on the risk profile, it is appropriate that more stringent remuneration policies, including specific provisions on their variable remuneration, are applied.

14. The gender neutral remuneration policy for all staff, including identified staff, must be consistent with and promote sound and effective risk management. The remuneration policy should be consistent with the long-term strategy of the investment firm, including the overall business strategy, the corresponding risk strategy and appetite.

15. To set the appropriate incentives for long-term oriented and prudent risk taking, the remuneration policy and practices need to be transparent to staff regarding the fixed remuneration, the variable remuneration and the award criteria used. Fixed remuneration should be permanent, predetermined, non-discretionary and non-revocable. Variable remuneration should be based on performance and in exceptional cases other conditions. Opaque remuneration policies, e.g. where the conditions for payments are not transparent, are discretionary or where adjustments of the remuneration depend unilaterally on the sole discretion of the investment firm, could have unforeseen effects on staff's behaviour in terms of risk-related decisions and are therefore not consistent with the above principles.

16. Implementing a sound remuneration policy is the responsibility of the management body and, where applicable, the remuneration committee. In practice, the development of a remuneration policy needs to be supported by internal control functions and relevant corporate functions to ensure that appropriate performance and risk measurement tools are used and that contracts between investment firms and staff ensure that the remuneration policies are applied. Moreover, business units need to be involved in the development of the remuneration policy to ensure that appropriate incentives, in particular for identified staff within the business units, are set.

17. The corporate bodies which have the competencies to approve the remuneration policy may differ among countries due to national corporate law. Additionally, in some countries the corporate body that approves the remuneration policy of the management body may differ from

the one that approves the remuneration policy for identified staff in business areas and identified staff in control functions. In addition, some investment firms might be directed by only one person. For these reasons, these guidelines should be read together with the relevant national legal provisions.

18. In accordance with the IFD, investment firms have to apply the remuneration requirements at an individual and at a consolidated basis. This includes all subsidiaries of an investment firm within the prudential scope of consolidation, including in third countries, unless the application of the requirement would be unlawful in a subsidiary located in a third country.

Gender neutral remuneration policies

19. The principle of equal pay for male and female workers for equal work or work of equal value is laid down in Article 157 of the Treaty on the Functioning of the European Union (TFEU). The IFD requires investment firms to ensure that they apply a gender neutral remuneration policy for all staff, including their risk takers, i.e. a remuneration policy based on equal pay for male and female workers for equal work or work of equal value. The same principle applies to workers of all diverse genders when implemented into national law.

20. According to Article 157 TFEU, equal pay for equal work or work of equal value includes the ordinary basic or minimum wage or salary and any other consideration, whether in cash or in kind, which the worker receives directly or indirectly, in respect of their employment, from their employer. The TFEU calls for further measures to ensure equal opportunities and equal treatment of men and women in matters of employment and occupation. However, the principle of equal treatment shall not prevent Member States from maintaining or adopting measures providing for specific advantages in order to make it easier for the underrepresented sex [1] to pursue a vocational activity or to prevent or compensate for disadvantages in professional careers.

21. Where the remuneration of most of the staff is subject to collective bargaining, it is easier to monitor remuneration policies are applied in a gender neutral way so that contracts are applicable independent of the gender of staff. Ensuring gender neutrality with regard to individually agreed contracts is more complex and requires a more sophisticated approach.

22. Member States and employers, in line with the Charter of Fundamental Rights of the European Union, European Convention for the Protection of Human Rights and Fundamental Freedoms and the Universal Declaration of Human Rights, should strive to avoid any discrimination within the conditions of employment, including discrimination based on gender.

23. Consequently, in addition to ensuring equal pay for the same position or positions of equal value, it is also necessary to ensure equal opportunities for all genders. Equal career perspectives help to improve the representation of the underrepresented gender in the

[1] While Article 157 TFEU uses the term ‘underrepresented sex’, these guidelines, in line with the terminology of the CRD, uses also the term ‘underrepresented gender’, both terms have the same meaning for the purpose of these guidelines.

management body of investment firms in the longer run by facilitating the existence of a diverse pool of candidates for such positions, e.g. within investment firms' senior management.

Proportionality

24. When complying with the remuneration provisions, investment firms should apply them in a manner that is appropriate to the investment firms' activities, nature, scale and complexity. This proportionality principle aims to match remuneration policies and practices consistently with the investment firms' risk profile, risk appetite and strategy, so that the objectives of the obligations are more efficiently achieved.

25. With regard to the requirement under Article 32(1)(j) of IFD that investment firms pay out at least 50% of the variable remuneration of identified staff in instruments and that they defer the pay-out for a part of the variable remuneration, the co-legislator has introduced the possibility that Member States waive the application of those provisions for investment firms that have total assets under a certain threshold set within national law and for staff with a variable remuneration of EUR 50,000 or below, when it does not represent more than one quarter of the staff member's total annual remuneration. For this purpose, the amounts of variable and fixed remuneration have to be calculated in each financial year using the amounts paid for the previous financial year. For example, to determine if the waiver can be applied to the variable remuneration of the financial year ending 31.12.2022, the investment firm should calculate the fixed remuneration awarded for 2022 and the variable remuneration awarded in 2023 for 2022, including all amounts for performance periods that ended in 2022, which may include performance periods that are longer than one year. When implementing the quantitative thresholds, Member States have some flexibility regarding the amounts, as specified further in the IFD. While the implementation of waivers and thresholds is at the discretion of Member States, the guidelines contain some procedural requirements on their application.

Identification of staff

26. All investment firms subject to remuneration requirements under IFD have to identify all staff whose professional activities have a material impact on the risk profile of the individual investment firms or the assets they manage. The guidelines aim at ensuring that the identification process of staff whose professional activities have a material impact on the risk profile of the investment firms or the assets they manage is consistently applied by all investment firms. The IFD requires investment firms to identify such staff in any case before the requirements are applied in a proportionate way to the different categories of identified staff. This also holds true if identified staff benefit from the application of waivers under Article 32(4) IFD.

27. In line with Article 25(4) IFD, the identification has also to be performed at a consolidated level. The primary responsibility for the identification process for the consolidated level lies with the Union parent undertaking. To ensure that the identification can be performed at the consolidated level, it is appropriate to require that subsidiaries should actively participate in the identification process by providing the necessary information to assess the impact of staff on

the risk profile of the investment firm or the assets it manages at a consolidated level. Staff identified at the consolidated level are subject to the remuneration requirements under IFD at the consolidated level, even if they are employed by a subsidiary that is not subject to the specific remuneration requirements under IFD on an individual level.

28. Notwithstanding the definition of criteria within the IFD and respective Commission Delegated Regulation, investment firms are obliged under the IFD to identify all staff whose professional activities have a material impact on the risk profile of the investment firm or the assets it manages and therefore investment firms should consider the need to apply additional internal criteria which ensure that the specific risk profile and internal organisation of the investment firm are taken into account.

Capital base

29. Investment firms must have a sound capital base. Remuneration represents an important cost factor for investment firms and remuneration payments influence directly the investment firm's capital base and liquidity. There is also an indirect influence on the capital base (i.e. the impact of the remuneration policy on the risks taken for which capital is required). If an investment firm falls short of its capital targets, priority is to be given to building up the necessary capital or solvency buffer and a conservative remuneration policy needs to be pursued, particularly regarding the variable remuneration. To ensure that remuneration does not endanger the financial stability of the investment firm, remuneration must also be taken into account for capital and liquidity planning purposes.

30. Article 39(2)(g) of IFD empowers competent authorities to require investment firms to limit variable remuneration as a percentage of net revenues where that remuneration is inconsistent with the maintenance of a sound capital base.

Categories of remuneration

31. In accordance with Article 30 of IFD, it must be ensured that the fixed and variable components of total remuneration are set in a way that allows a fully flexible policy on variable remuneration and reflects the business strategy of the investment firm and associated risks. Remuneration is either fixed or variable; there is no third category of remuneration. A clear distinction between those two types of remuneration is necessary to ensure that compliance with requirements on the variable remuneration of identified staff can be monitored and supervised.

32. Variable remuneration of identified staff should provide incentives for prudent risk taking in the long term and for sound risk management. Fixed remuneration should primarily reflect the relevant professional experience and organisational responsibility of staff and provide for a stable source of income.

Requirements for variable remuneration

33. Variable remuneration provides an incentive for staff members to pursue the goals and interests of the investment firm and enables them to share in its success. It is also an element of cost flexibility for investment firms. Provided that there is no incentive to assume inappropriate or excessive risks, an appropriate level of variable remuneration can benefit all stakeholders of an investment firm. A variable component linked to performance, the deferral of variable remuneration and pay-out in financial instruments can have a positive effect on 'risk-sharing' in the longer run, incentivising prudent behaviour and ensuring a safe and sound performance of the investment firm.

Risk alignment

34. It is necessary to counterbalance the incentives of variable remuneration for risk taking with measures to incentivise sound risk management. Variable remuneration needs to be aligned with the risk-related performance over time, in particular for identified staff. Otherwise such arrangements can create a 'heads I win, tails I still win' approach to risk, which encourages more risk taking than would likely be preferred by the investment firm's shareholders or creditors. To ensure a sound risk alignment of variable remuneration, staff should also not be able to transfer the downside risks to another party, e.g. through hedging or insurance.

35. Any form of variable remuneration should always be consistent with and promote sound and effective risk management. The effectiveness of risk alignment would be significantly weakened if investment firms made excessive use of retention bonuses or guaranteed variable remuneration. Therefore, investment firms need to be able to justify the use of any variable remuneration element, including retention bonuses, guaranteed variable remuneration and severance payments.

36. Remuneration has a direct or indirect influence on staff's behaviour. Variable remuneration may encourage staff to take undesirable, irresponsible and excessive risks or to sell unsuitable products in the hope of generating more turnover or making more profit in the short run, if such action would lead to an increase of staff's variable remuneration. Furthermore, staff members may be tempted to game with or manipulate information with a view to making their (measured) performance look better. For example, if the variable part of the remuneration consists predominantly of remuneration instruments that are paid out immediately, without any deferral or ex post risk adjustment mechanisms (e.g. malus or clawback), or are based on a formula that links variable remuneration only to current year revenues rather than risk-adjusted profit, there are strong incentives for staff to shy away from conservative valuation policies, to ignore concentration risks, to rig the internal transfer pricing system in their favour and to ignore risk factors, such as liquidity risk and concentration risk, that could place the investment firm under stress in the future. By connecting risk management provisions to the remuneration policy, the aforementioned risks can be counterbalanced.

37. The guidelines on risk alignment contain the general provisions that should apply to investment firms and their staff and the specific requirements that investment firms have to apply at least to the individual remuneration packages of identified staff under Articles 30 and 32 of the IFD.

Investment firms can also apply these more specific requirements and their specification within these guidelines to additional categories of staff.

38. The risk alignment process and the award process should be transparent to ensure that they have an impact on staff's behaviour as intended.

39. So-called ex ante risk adjustments are applied when the remuneration is awarded in a way that considers current and future risks and has an immediate effect on the variable remuneration awarded and on staff's risk taking behaviour.

40. Ex-post risk adjustments ensure that staff are rewarded in line with the sustainability of the performance in the long term, which is the result of decisions taken in the past. A framework for ex post risk adjustments is always necessary, also in case of multi-year accrual periods, because at the time remuneration is awarded, the ultimate performance cannot be assessed without uncertainty. Ex post risk adjustments are achieved by different means, in particular the application of deferral, malus and clawback and the pay-out in suitable instruments.

41. In order to ensure that the risk-adjusted performance is appropriately reflected in the variable remuneration, investment firms need to measure risks and performance and use a mix of different qualitative and quantitative criteria for their measurement to ensure that overall the assessment outcome is appropriate and weaknesses of single criteria are counterbalanced. This applies at all stages, the setting of the bonus pool, the actual award of remuneration and the application of ex-post risk adjustments. There are different categories of performance criteria: relative, absolute, internal and external.

42. Absolute performance measures are measures set by the investment firm on the basis of its own strategy, including its risk profile and risk appetite. Relative performance measures are measures that compare performance with peers, either 'internal' peers (i.e. within the organisation) or 'external' (i.e. similar investment firms). The advantage of absolute measures is that they are easier to set and monitor. Relative measures could encourage excessive risk taking and therefore need always to be supplemented by other metrics and controls, including the use of prudent judgmental analysis during the award process.

43. In a period of sector wide positive financial performances, external relative measures could lead to increased risk taking and a herd mentality, with a potential negative impact on the financial stability of the financial sector. In a downturn economic cycle where most investment firms perform poorly, relative external measures may lead to positive measurements of a per se negative outcome and thus to an insufficient contraction of the investment firm's total variable remuneration.

44. Similarly, internal (e.g. profits) and external (e.g. share price) variables come with both advantages and disadvantages that should be balanced carefully. Internal performance measures are able to generate more involvement of the staff members if they can influence the outcome with their own behaviour. On the other hand, such measures can be manipulated and can create distorted outcomes on a short-term basis. External performance measures are less

subject to the risk of manipulation, although, for example, attempts to artificially increase the stock price can still occur.

45. Every criterion used has its risks, limitation and advantage. Investment firms need to take these into account and weight them carefully when determining the performance and risk criteria at every level (i.e. the investment firm, the business area and the individual) and use an appropriate mix to minimise the risks and assess the performance as objectively as possible.

Pay-out process

46. The IFD requires that class 2 investment firms pay at least 50% of variable remuneration in shares, equivalent ownership rights, share-linked or equivalent non-cash instruments, certain eligible AT1 and AT2 instruments or other instruments defined within the RTS on instruments and non-cash instruments which reflect the instruments of the portfolios managed. Some investment firms and staff benefit from waivers of those requirements. When an investment firm does not issue any of those instruments, the competent authority may approve that it uses alternative arrangements which fulfil the same objectives. The awarded instruments are subject to retention periods.

47. At least 40% of variable remuneration of identified staff is subject to deferral arrangements unless the investment firm or staff member benefits from waivers under Article 32(4) IFD.

48. The above requirements regarding the pay-out of variable remuneration should ensure that the variable remuneration is aligned with the risks of the investment firm in the long term and that ex post risk adjustments can be applied as appropriate.

49. A deferral schedule is key to ensuring risk alignment effects in a remuneration package, since it allows for parts of the remuneration to be adjusted for risk outcomes over time through ex post risk adjustments. The ratio of deferred remuneration to variable remuneration and the deferral period needs to be tailored to the long-term impact of the category of identified staff throughout the business cycle and therefore arrangements may differ between different categories of identified staff and will also depend on the investment firm’s business model.

50. Although variable remuneration should already be aligned with risk through ex ante risk adjustments, due to the uncertainty about the assessment and future development of risks, ex post risk adjustments are needed to keep incentives fully aligned over an appropriate time period. This can only be achieved where an appropriate part of the variable remuneration is deferred. In particular in Member States where the application of malus or clawback may not be in line with the general principles of national contract and labour law, investment firms should carefully design the instruments used for the award, the deferral and retention scheme in order to ensure that the requisite ex post risk adjustments are reflected, e.g. in price changes of the instruments.

51. In the absence of deferral arrangements, longer retention periods can help to establish some risk alignment. However, it is important to highlight that the upfront payment of instruments as

variable remuneration, even if the retention period equals the applied deferral period, is not equivalent to the deferral of instruments.

52. Retention periods affect the risk taking incentives of staff members only by extending the period during which implicit adjustments can take place. Instruments paid upfront belong to the staff member (they are vested rights) which imply that no malus clauses (i.e. no reduction of the number of instruments that will be received) can be applied to them. Even though clawback may be applicable, the ability to apply ex post risk adjustment will be weakened and is without prejudice to the national labour and contract laws.

53. Unlike retained instruments, deferred instruments allow for the application of explicit ex post risk adjustments via malus arrangements, e.g. determined by the back-testing of the underlying performance, possibly leading to a reduction of the number of instruments that will eventually vest and be paid out.

54. Explicit ex post risk adjustments should not lead to an increase of the variable remuneration as this could provide for incentives to take more risk than that which can be considered prudent from a supervisory point of view.

55. When the variable remuneration takes the form of instruments, the final monetary value received by staff depends also on the market prices or the fair value of these instruments. This implicit adjustment of remuneration due to changes of the market price of listed instruments or the fair value of non-listed instruments is not related to any explicit decision of the investment firm, but inherent to the instruments used for the award. Market prices respond to many factors and are without additional ex post risk adjustments not sufficient to align the variable remuneration with the risks taken in the long term. The same is true for the fair value, which in addition is less objective than an observed market price.

State aid and government support

56. Investment firms receiving extraordinary public financial support are often obliged to return the funds received and also to increase their capital base in line with recovery plans. Remuneration policies must be aligned with these circumstances and in such cases, in accordance with the IFD, the members of the management board should not receive any variable remuneration and under certain conditions, the variable remuneration of other staff is limited to a portion of net revenue. If in such situations variable remuneration is awarded, an even stronger risk alignment seems to be appropriate in order to contribute to the protection of the capital base and aid the recovery of the investment firm.

Supervisory review by competent authorities

57. The IFD requires competent authorities to ensure that investment firms comply with the requirements under the IFD. As part of this, competent authorities need to review the investment firms' remuneration policies and practices and their compliance with the IFD provisions and these guidelines.

58. Competent authorities should apply risk-based supervision; resources should be directed primarily to those investment firms and areas that pose most risks, taking into account their size and the nature, scope and complexity of their activities. These guidelines provide for specific areas which should be reviewed as part of the supervisory activities of competent authorities. The EBA guidelines on the supervisory review and evaluation process[2] specify further the supervisory review.

59. The assessment methodologies of competent authorities may include both on-site and off-site controls, including the examination of information and data and dedicated meetings as appropriate with the investment firms' management body, senior management and other relevant staff, in order to collect additional information and data on remuneration policies, remuneration structures and governance arrangements. The review should identify the potential implementation gaps and non-compliant practices. All findings need to be appropriately addressed to ensure that investment firms' remuneration policies and practices comply with the respective requirements in the IFD and IFR as further specified in these guidelines.

[2] https://www.eba.europa.eu/regulation-and-policy/supervisory-review-and-evaluation-process-srep-and-pillar-2

EBA EUROPEAN BANKING AUTHORITY

EBA/GL/2021/13

22 November 2021

Guidelines

on sound remuneration policies under Directive (EU) 2019/2034

EBA EUROPEAN BANKING AUTHORITY

1. Compliance and reporting obligations

Status of these guidelines

1. This document contains guidelines issued pursuant to Article 16 of Regulation (EU) No 1093/2010[3]. In accordance with Article 16(3) of Regulation (EU) No 1093/2010, competent authorities and financial investment firms must make every effort to comply with the guidelines.

2. Guidelines set the EBA view of appropriate supervisory practices within the European System of Financial Supervision or of how Union law should be applied in a particular area. Competent authorities as defined in Article 4(2) of Regulation (EU) No 1093/2010 to whom guidelines apply should comply by incorporating them into their practices as appropriate (e.g. by amending their legal framework or their supervisory processes), including where guidelines are directed primarily at investment firms.

Reporting requirements

3. In accordance with Article 16(3) of Regulation (EU) No 1093/2010, competent authorities must notify the EBA as to whether they comply or intend to comply with these guidelines, or otherwise with reasons for non-compliance, by 16.05.2022. In the absence of any notification by this deadline, competent authorities will be considered by the EBA to be non-compliant. Notifications should be sent by submitting the form available on the EBA website with the reference 'EBA/GL/2021/13'. Notifications should be submitted by persons with appropriate authority to report compliance on behalf of their competent authorities. Any change in the status of compliance must also be reported to EBA.

4. Notifications will be published on the EBA website in line with Article 16(3).

[3] Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC, (OJ L 331, 15.12.2010, p.12).

2. Subject matter, scope and definitions

Subject matter

5. These guidelines specify further, in accordance with Article 26(4) and Article 34(3) of Directive 2019/2034, the sound and gender neutral remuneration policies that investment firms should have in place for all staff and for staff whose professional activities have a material impact on the risk profile of investment firms or the assets they manage and facilitate the implementation of the derogations under paragraphs 4, 5, 6 of Article 32 of Directive (EU) 2019/2034.

6. While investment firms are required to have remuneration policies for all staff, additional requirements apply to remuneration policies and the variable remuneration of identified staff. Investment firms may apply on their own initiative the provisions of these guidelines concerning identified staff to all their staff.

Addressees

7. These guidelines are addressed to competent authorities as referred to in Article 4 (2), point (viii) of Regulation No 1093/2010 and as defined in Article 3 (1), point 5 of Directive (EU) 2019/2034, and to financial institutions as referred to in Article 4 (1) of Regulation (EU) 1093/2010 that are investment firms as defined in Article 4(1)(1) of Directive 2014/65/EU, that do not fall under Article 2 (2) of Directive (EU) 2019/2034 and do not meet all of the conditions to qualify as small and non-interconnected investment firms under Article 12(1) of Regulation (EU) 2019/2033.

Scope of application

8. These guidelines apply on an individual and consolidated basis within the scope set out in Article 25 of Directive 2019/2034/EU and Article 7 of Regulation 2019/2033/EU.

Definitions

9. The terms used and defined in Directive 2019/34/EU, Directive 2014/65/EU and Regulation (EU) No 2033/2019 have the same meaning in the guidelines. In addition, for the purposes of these guidelines, the following definitions apply:

Remuneration	means all forms of fixed and variable remuneration and includes payments and benefits, monetary or non-monetary, awarded directly to staff by or on behalf of investment firms in exchange for professional services rendered by staff, carried interest payments

	within the meaning of Article 4(1)(d) of Directive 2011/61/EU[4], and other payments made via methods and vehicles which, if they were not considered as remuneration, would lead to a circumvention[5] of the remuneration requirements of Directive (EU) 2019/2034.
Fixed remuneration	means payments or benefits for staff which comply with the conditions for its award set out in section 7.
Variable remuneration	means all remuneration that is not fixed.
Routine employment packages	means ancillary components of remuneration that are obtainable for a wide population of staff or staff in specified functions based on predetermined selection criteria, including, for example, healthcare, child care facilities or proportionate regular pension contributions on top of the mandatory regime and travel allowance.
Retention bonus	means variable remuneration awarded on the condition that staff stay in the investment firm for a predefined period of time.
Staff	means all employees of an investment firm and its subsidiaries on a consolidated basis and all members of their respective management bodies in its management function and in its supervisory function.
Identified staff	means staff whose professional activities have a material impact on the investment firm's individual or the group's risk profile or of the assets that it manages in accordance with the criteria set out in Article 30(1) of Directive (EU) 2019/2034, the Commission Delegated Regulation adopted under the empowerment within the last subparagraph of Article 30(4) of this Directive (RTS on identified staff) and, where appropriate to ensure a complete identification of staff whose professional activities have a material impact on the risk profile, additional criteria defined by the investment firm.
Prudential consolidation	means the application of the prudential rules set out in Article 25(4) of Directive (EU) 2019/2034 and Article 7 of Regulation (EU) 2019/2033.
Underrepresented gender	means the less represented male or female gender.
Gender pay gap	means the difference between the average gross hourly earnings of men and women expressed as a percentage of the average gross hourly earnings of men.
Union parent undertaking	means a Union parent investment firm, Union parent investment holding company or Union parent mixed financial holding company that is required to abide by the prudential requirements on the basis of the consolidated situation in accordance with Article 7 of Regulation (EU) 2019/2033.

[4] Directive 2011/61/EU …. of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulation (EC) No 1060/2009 and (EU) No 1095/2010 (AIFMD).

[5] Regarding circumvention please refer to section 10.2 of these guidelines.

Consolidating institution	means the institution or investment firm which is required to abide by the prudential requirements on the basis of the consolidated situation in accordance with Part One, Title II, Chapter 2 of Regulation (EU) No 575/2013 and Article 109 of Directive 2013/36/EU or Article 7 of Regulation (EU) 2019/2033. Any reference to the term 'consolidating institution' includes the Union parent undertaking.
Bonus pool	means the maximum amount of variable remuneration which can be awarded in the award process set at the level of the investment firm or an investment firm's business unit.
Accrual period	means the period of time for which the performance is assessed and measured for the purposes of determining an award of variable remuneration.
Non-revolving multi-year accrual period	means a multi-year accrual period that does not overlap with other multi-year accrual periods.
Award	means the granting of variable remuneration for a specific accrual period, independently of the actual point in time where the awarded amount is paid.
Vesting	means the effect by which the staff member becomes the legal owner of the variable remuneration awarded, independent of the instrument which is used for the payment or if the payment is subject to additional retention periods or clawback arrangements.
Upfront payments	means payments which are made immediately after the accrual period and which are not deferred.
Deferral period	means the period of time between the award and the vesting of the variable remuneration during which staff are not the legal owner of the remuneration awarded.
Instruments	means those financial instruments, other contracts or vehicles that fall within one of the categories referred to in Article 32(1)(j) of Directive (EU) 2019/2034.
Retention period	means a period of time after the vesting of instruments which have been awarded as variable remuneration during which they cannot be sold or accessed.
Malus	means an arrangement that permits the investment firm to reduce the value of all or part of deferred variable remuneration based on ex post risk adjustments before it has vested.
Clawback	means an arrangement under which the staff member has to return ownership of an amount of variable remuneration paid in the past or which has already vested to the investment firm under certain conditions.
Share-linked instruments	means those instruments whose value is based on the value of the stock and that have the share value as a reference point, e.g. stock appreciation rights, types of synthetic shares.
Shareholders	means a person who owns shares in an investment firm or, depending on the legal form of an investment firm, other owners or members of the investment firm.

Severance payments	means payments relating to the early termination of a contract, i.e. in the case of temporary contracts a termination before the end date of the contract and in the case of indefinite contracts before the contractual or legal retirement, by an investment firm or its subsidiaries.

3. Implementation

Date of application

10. These guidelines apply from 30 April 2022.

Transitional provisions

11. Investment firms should implement any adjustments of their remuneration policies by 30 April 2022 and update the required documentation accordingly. Where shareholder approvals are required for such revisions, approvals should be requested before 30 June 2022. Without prejudice to the implementation of Directive (EU) 2019/2014 into national law, the remuneration policy should be applied in line with these guidelines for the performance year starting after 31 December 2021.

EBA EUROPEAN BANKING AUTHORITY

4. Guidelines

Title I - Remuneration policies

1. Remuneration policies for all staff

12. In accordance with Article 26 of Directive (EU) 2019/2034, investment firms are required to have in place a remuneration policy for all staff, taking into account the criteria within Articles 28 to 33 of this Directive and these guidelines. The remuneration policy for all staff should be gender neutral, i.e. staff, independent of their gender, should be equally remunerated for equal work or work of equal value in line with point 12 of Article 3(1) of Directive (EU) 2019/2034 and Article 157 TFEU. There should also be a gender neutral approach to pay increases and career progression.

13. The remuneration policy should specify all components of remuneration and include also the pension policy, including, where relevant, the framework for early retirements. The remuneration policy should also set a framework for other persons acting on behalf of the investment firm (e.g. tied agents), ensuring that the payments made are providing incentives for prudent risk taking and do not provide for any incentive for excessive risk taking or the mis-selling of products.

14. The fixed remuneration of staff should reflect their professional experience and organisational responsibility taking into account the level of education, the degree of seniority, the level of expertise and skills, the constraints (e.g. social, economic, cultural or other relevant factors) and job experience, the relevant business activity and remuneration level of the geographical location. The fixed remuneration should be gender neutral in the same way as the variable remuneration.

15. Where an investment firm benefits from extraordinary public financial support, the investment firm should ensure that the remuneration policy for all staff is consistent with the requirements under Article 31 of Directive (EU) 2019/2034.

16. The investment firm's remuneration policy for all staff should be consistent with the objectives of the investment firm's business and risk strategy, including environmental, social and governance (ESG[6]) risk-related objectives, corporate culture and values, risk culture, including with regard to environmental, social and governance (ESG) risk factors, long-term interests of the investment firm, and the measures used to avoid conflicts of interest, encourage prudent risk taking and responsible business conduct. Changes of such objectives and measures should be taken into account when updating the remuneration policy. Investment firms should ensure that remuneration practices are aligned with their overall risk appetite, taking into account all

[6] See also Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector

risks, including reputational risks and operational risks resulting from the mis-selling of products. Investment firms should also take into account the long-term interests of shareholders or owners, depending on the legal form of the investment firm.

17. Investment firms should be able to demonstrate to the competent authorities that the remuneration policy and practices are consistent with and promote sound and effective risk management.

18. Where variable remuneration is awarded, such awards should be based on the investment firms', staff's and, where applicable, business units' performance and take into account the risks taken. The remuneration policy should make a clear distinction with regard to the variable remuneration and the performance assessment between the operating business, corporate and control functions. Investment firms should consider which elements of the remuneration policy on the variable remuneration of identified staff under Article 32 of IFD should be included in the remuneration policy for all staff.

19. The remuneration policy should be consistent with the requirement for an investment firm to have a sound capital base. The remuneration policy should also take into account possible restrictions on distributions under Article 39 of Directive (EU) 2019/2034.

20. The remuneration policy should contain:

    a. the performance objectives for the investment firm, business areas and staff;

    b. the methods for the measurement of performance, including the performance criteria;

    c. the structure of variable remuneration, including where applicable the instruments in which parts of the variable remuneration are awarded;

    d. the ex ante and ex post risk adjustment measures of the variable remuneration[7].

21. Investment firms should ensure that potential conflicts of interest caused by the pay-out of instruments as part of the variable or fixed remuneration are identified and managed. This includes ensuring that insider trading rules are complied with and that no measures are taken that can have a short-term impact on the share or instruments price.

22. Where remuneration policies or group remuneration policies are implemented in investment firms, including in their subsidiaries, and the staff of the investment firm are also the majority owners of the investment firm or the subsidiary, the remuneration policy should be adjusted to the specific situation of these investment firms or subsidiaries. For identified staff, the investment firm should ensure that the remuneration policy complies with the relevant requirements within Articles 30 and 32 of Directive (EU) 2019/2034 and these guidelines on an individual and where applicable consolidated level.

[7] Specific requirements for the remuneration of identified staff and its risk alignment are contained in Titles III and IV of these guidelines.

23. Without prejudice to any measures adopted by Member States[8] to prevent or compensate for disadvantages in professional careers of the underrepresented sex[9], the remuneration policy and all related employment conditions that have an impact on the pay per unit of measurement or time rate should be gender neutral, i.e. there should be no differentiation between staff of the male, female or diverse genders.

24. A gender neutral remuneration policy should ensure that all aspects of the remuneration policy are gender neutral, including the award and pay-out conditions for remuneration. Investment firms should be able to demonstrate that the remuneration policy is gender neutral.

25. When determining the pay per unit of measurement or time, investment firms should duly consider the remuneration awarded, working time arrangements, annual leave periods and other financial and non-financial benefits. Investment firms may use as a unit of measurement the annual gross remuneration of staff calculated on a full-time equivalent basis.

26. In order to monitor the application of gender neutral remuneration policies, investment firms should document appropriately the value of the position, e.g. by documenting job descriptions or defining wage categories, for all staff members or categories of staff and determine which positions are considered as having an equal value, e.g. by implementing a job classification system, taking into account at least the type of activities, tasks and duties assigned to the position or staff member. Where a job classification system is used for determining pay, it should be based on the same criteria for men, women and staff of diverse genders and so drawn up as to exclude any discrimination, including on grounds of gender.

27. Investment firms may consider in a gender neutral manner additional aspects when determining the remuneration of staff. Such aspects may include:

    a. educational, professional and training requirements, skills, effort and responsibility, work undertaken and the nature of tasks involved[10];

    b. the place of employment and its costs of living;

    c. the hierarchical level of the staff and if staff has managerial responsibilities;

    d. the level of formal education of staff;

    e. the scarcity of staff available in the labour market for specialised positions;

    f. the nature of the employment contract, including if it is temporary or a contract with an indefinite period;

[8] E.g. when implementing Directive 2006/54/EC

[9] While Article 157 TFEU uses the term 'underrepresented sex', these guidelines, in line with the terminology of the CRD, use also the term 'underrepresented gender', both terms have the same meaning for the purpose of this guideline.

[10] See also Commission recommendation of 7.3.2014 on strengthening the principle of equal pay between men and women through transparency

g. the length of professional experience of staff;

h. professional certifications of staff;

i. appropriate benefits, including the payment of additional household and child allowances to staff with spouses and dependent family members.

2. Governance of remuneration

2.1 Responsibilities, design, approval and oversight of the remuneration policy

28. The management body[11] in its supervisory function (hereafter 'supervisory function') should be responsible for adopting and maintaining the remuneration policy of the investment firm, and overseeing its implementation to ensure it is fully operating as intended. The supervisory function should also approve any subsequent material exemptions made for individual staff members and changes to the remuneration policy and carefully consider and monitor their effects. Any exemptions should not be based on gender considerations or other aspects that would be discriminating, should be well reasoned and should be in line with the remuneration requirements under national law.

29. The supervisory function should collectively have adequate knowledge, skills and experience with regard to remuneration policies and practices as well as of incentives and risks that can arise therefrom. This should include knowledge, skills and experience with regard to the mechanisms for aligning the remuneration structure to investment firms' risk profiles and capital structure.

30. The supervisory function should ensure that the investment firm's remuneration policies and practices are appropriately implemented and aligned with the investment firm's overall corporate governance framework, corporate and risk culture, risk appetite and the related governance processes.

31. Conflicts of interests with regard to the remuneration policy and remuneration awarded should be identified and appropriately mitigated, including by establishing objective award criteria based on the internal reporting system, appropriate controls and the four eyes principle. The remuneration policy should ensure that no material conflicts of interest arise, including for staff in control functions.

32. The remuneration policy and practices and the procedures to determine them should be clear, well documented and transparent. Proper documentation on the decision-making process (e.g.

[11] Different management body structures can be observed in European countries. In some countries a unitary structure is common, i.e. supervisory and management functions of the board are exercised by only one body. In other countries a dual structure is common, with two independent bodies being established, one for the management function and the other for the supervision of the management function.

minutes of relevant meetings, relevant reports, and other relevant documents) and the reasoning behind the remuneration policy should be maintained.

33. The supervisory and management functions and, where established, the remuneration and the risk committees should work closely together and ensure that the remuneration policy is consistent with and promotes sound and effective risk management.

34. The remuneration policy should provide for an effective framework for performance measurement, risk adjustment and the linkages of performance to reward.

35. The compliance function and the risk management function, where established,[12] or staff entrusted with the performance of risk management procedures (hereinafter it should be understood that a reference to the risk management function applies in the same way to staff entrusted with risk management procedures, where such a function is not established), should provide effective input in accordance with their roles into the setting of bonus pools, performance criteria and remuneration awards where those functions have concerns regarding the impact on staff behaviour and the riskiness of the business undertaken.

36. The supervisory function should determine and oversee the remuneration of the members of the management function and, if the remuneration committee referred to in section 2.4 has not been established, oversee directly the remuneration of the senior officers in the independent control functions, including the compliance function and the risk management function, where established.

37. The supervisory function should take into account the input provided by all competent corporate functions and bodies (e.g. committees, control functions[13], human resources, legal, strategic planning, budget function, etc.) and business units about the design, implementation and oversight of the investment firm's remuneration policies.

38. The human resources function should participate in and inform on the drawing up and the evaluation of the remuneration policy for the investment firm, including the remuneration structure, the aspect of gender neutrality, remuneration levels and incentive schemes, in a way that would not only attract and retain the staff the investment firm needs, but also ensure that the remuneration policy is aligned with the investment firm's risk profile.

39. The risk management function should assist in and inform on the definition of suitable risk-adjusted performance measures (including ex post adjustments), as well as with assess how the variable remuneration structure affects the risk profile and culture of the investment firm. The risk management function should validate and assess risk adjustment data as well as be invited to attend the meetings of the remuneration committee on this matter.

40. The compliance function should analyse how the remuneration policy affects the investment firm's compliance with legislation, regulations, internal policies and risk culture and should

[12] See EBA guidelines on internal governance for investment firms

[13] See EBA guidelines on internal governance for investment firms

report all identified compliance risks and issues of non-compliance to the management body, both in its management and supervisory functions. The findings of the compliance function should be taken into account by the supervisory function during the approval, review procedures and oversight of the remuneration policy.

41. The internal audit function, where established, should carry out an independent review of the design, implementation and effects of the investment firm's remuneration policies on its risk profile and the way these effects are managed in line with the guidelines provided in section 2.5. The review may be performed by another group entity or outsourced to an external party.

42. Within a group context, the competent functions within the Union parent undertaking and subsidiaries should interact and exchange information as appropriate. Investment firms should also exchange information as appropriate with their consolidating institution, in situations where the consolidating institution is subject to Directive 2013/36/EU.

2.2 Shareholders' involvement

43. Depending on the investment firm's legal form and on the applicable national law, the approval of an investment firm's remuneration policy and, where appropriate, decisions relating to the remuneration of members of the management body and other identified staff may also be assigned to the shareholders' meeting in accordance with national company law[14]. The shareholders' vote may be either consultative or binding.

44. Where the approval of the remuneration of individual members of the management body and other identified staff is assigned to shareholders, shareholders should approve all components of remuneration, including severance payments. Where the approval of the remuneration policy is subject to approval by the shareholders, they should also either approve ex ante the maximum amount of the payments that can be awarded to the management body and other identified staff in the event of early termination of a contract or criteria for the determination of such amounts.

45. In order that shareholders can make informed decisions in line with paragraphs 43 and 44, the supervisory function should ensure that the investment firm provides them with adequate information regarding the remuneration policy designed to help them to assess the incentive structure and the extent to which risk taking is being incentivised and controlled as well as the overall cost of the remuneration structure. Such information should be provided well in advance of the relevant shareholders' meeting. Detailed information on remuneration policies and on their modifications, on procedures and decision-making processes to set a remuneration package should be provided and include the following:

    a. the remuneration components;

[14] See also Shareholders Rights Directive 2007/36, as amended by Directive 2017/828, Articles 9a and 9b.

b. main characteristics and objectives of the remuneration packages and their alignment with the business and risk strategy, including the risk appetite and corporate values of the investment firm;

c. how it is ensured that the remuneration policy is gender neutral;

d. how the points under (b) are taken into account in ex ante/ex post adjustments, in particular for identified staff.

46. The supervisory function remains responsible for the proposals submitted to the shareholders' meeting, as well as for the actual implementation and oversight of any changes to the remuneration policies and practices.

2.3 Setting up a remuneration committee

47. Unless otherwise specified by national law, an investment firm with on and off-balance-sheet assets valued on average at more than EUR 100 million over the four-year period immediately preceding the given financial year must establish a remuneration committee to advise the management body in its supervisory function and to prepare the decisions to be taken by this body.

48. The remuneration committee might be established at group level, including in situations where the consolidating institution is subject to Directive 2013/36/EU. The provisions regarding the composition of the remuneration committee specified in section 2.4.1. apply also if the committee is established at group level.

49. Where no remuneration committee has to be established, the provisions of these guidelines concerning the remuneration committee should be construed as applying to the supervisory function.

2.3.1 Composition of the remuneration committee

50. In line with Article 33(1) of Directive (EU) 2019/2034, the remuneration committee consists of members of the management body that do not have any executive function and, where applicable, employee representatives. Only those staff members are considered as members of the remuneration committee, even if other staff were to participate at their meetings. The remuneration committee must be gender balanced.

51. The chair and the majority of members of the remuneration committee should qualify as independent[15]. If employee representation on the management body is provided for by national law, it must include one or more employee representatives. Where there is an insufficient number of independent members, investment firms should take particular care

[15] Independence as set out in the EBA guidelines on internal governance point 5.6 and see also the joint EBA-ESMA guidelines on the assessment of the suitability of members of the management body and key function holders

when implementing other measures to limit conflicts of interest in decisions on remuneration issues.

52. Members of the remuneration committee should have collectively appropriate knowledge, expertise and professional experience concerning remuneration policies and practices, risk management and control activities, namely with regard to the mechanism for aligning the remuneration structure to investment firms' risk and capital profiles.

2.3.2 Role of the remuneration committee

53. The remuneration committee should:

    a. be responsible for the preparation of decisions on remuneration to be taken by the supervisory function, in particular regarding the remuneration of the members of the management body in its management function as well as of other identified staff;

    b. provide its support and advice to the supervisory function on the design of the investment firm's remuneration policy, including that such remuneration policy is gender neutral and supports the equal treatment of staff of different genders;

    c. support the supervisory function in overseeing the remuneration policies, practices and processes and the compliance with the remuneration policy and the requirement for the remuneration policy to be gender neutral;

    d. check whether the existing remuneration policy is still up to date and, if necessary, make proposals for changes;

    e. review the appointment of external remuneration consultants that the supervisory function may decide to engage for advice or support;

    f. ensure the adequacy of the information provided to shareholders on remuneration policies and practices;

    g. assess the mechanisms and systems adopted to ensure that the remuneration system properly takes into account all types of risks, liquidity and capital levels and that the overall remuneration policy is gender neutral, is consistent with and promotes sound and effective risk management and is in line with the business strategy, objectives, corporate culture and values, risk culture and the long-term interest of the investment firm;

    h. assess the achievement of performance targets and the need for ex post risk adjustment, including the application of malus and clawback arrangements;

    i. review a number of possible scenarios to test how the remuneration policies and practices react to external and internal events, and back-test the criteria used for determining the award and the ex ante risk adjustment based on the actual risk outcomes.

54. Where the investment firm has established a remuneration committee, the remuneration of the senior officers in the compliance functions, and the risk management, audit functions where established, should be directly overseen by the remuneration committee. The same applies to staff who are entrusted with the performance of risk management procedures, where no risk management function has been established. The remuneration committee should make recommendations to the supervisory function on the design of the remuneration package and amounts of remuneration to be paid to the senior staff members in the control functions.

2.3.3 Process and reporting lines

55. The remuneration committee should:

    a. have access to all data and information concerning the decision-making process of the supervisory function on the remuneration policies and practices design and implementation, oversight and review;

    b. have adequate financial resources and unfettered access to all information and data from independent control functions, including risk management;

    c. ensure the proper involvement of the independent control and other relevant functions (e.g. human resources, legal and strategic planning) within the respective areas of expertise and where necessary seek external advice.

56. The remuneration committee should collaborate with other committees of the supervisory function whose activities may have an impact on the design and proper functioning of remuneration policies and practices (e.g. risk, audit and nomination committees); and provide adequate information to the supervisory function, and, where appropriate, to the shareholders' meeting about the activities performed.

57. When established, the risk committee should, without prejudice to the tasks of the remuneration committee, examine whether incentives provided by the remuneration policies and practices take into consideration the investment firm's risk, capital, liquidity and the likelihood and timing of earnings.

58. A member of the risk committee should, where relevant, participate in the meetings of the remuneration committee, where both committees are established, and vice versa.

2.4 Review of the remuneration policy

59. The supervisory function and, where established, the remuneration committee should ensure that the remuneration policy and practices of the investment firm are subject to a central and independent internal review at least annually. The review should include an analysis if the remuneration policy is gender neutral.

60. Investment firms should monitor the development of the gender pay gap; in case of investment firms with 50 staff or more, the calculation should be done separately on a country-by-country basis for:

    a. identified staff, excluding members of the management body;

    b. members of the management body in its management function;

    c. members of the management body in the supervisory function; and

    d. other staff.

61. Where material differences between the average pay between male and female staff or male and female members of the management body exist, investment firms should document the main reasons, take appropriate actions where relevant or should be able to demonstrate that the difference does not result from a remuneration policy that is not gender neutral.

62. In groups of investment firms, a central review of compliance with the regulation, group policies, procedures and internal rules should also be performed by the Union parent undertaking.

63. Investment firms should perform the central and independent review on an individual basis. In a group, subsidiaries may rely on the review performed by the Union parent undertaking or institution, where the review performed on the consolidated basis included the investment firm and where the results are made available to the supervisory function of that investment firm.

64. Notwithstanding the responsibility of the management body in its supervisory function, the tasks of the periodic independent review of remuneration policies may be, partially or totally, externally outsourced by investment firms.[16]

65. As part of the central and independent internal review, investment firms should assess whether the overall remuneration policies, practices and processes:

    a. operate as intended (in particular, that approved policies, procedures and internal rules are being complied with; that the remuneration pay-outs are appropriate, in line with the business strategy; and that the risk profile, long-term objectives and other goals of the investment firm are adequately reflected);

    b. are compliant with national and international regulations, principles and standards; and

    c. are consistently implemented across the group and do not limit the investment firm's ability to ensure a sound capital base in line with section 6 of these guidelines.

[16] See EBA guidelines on outsourcing arrangements and Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive

66. The other relevant internal corporate functions (i.e. human resources, legal, strategic planning, etc.), as well as other key supervisory function committees (i.e. audit, risk and nominations committees) should be closely involved in reviewing the remuneration policies of the investment firm in order to assure alignment with the investment firms' risk management strategy and framework.

67. Where periodic reviews reveal that the remuneration policies do not operate as intended or prescribed or where recommendations are made, the remuneration committee, where established, or the supervisory function, should ensure that a remedial action plan is proposed, approved and timeously implemented.

68. The results of the performed internal review and actions taken to remedy any findings should be documented, either through written reports or through the minutes of the meeting of the relevant committees or the supervisory function, and made available to the management body, relevant committees and corporate functions.

2.5 Internal transparency

69. The remuneration policy of an investment firm should be internally disclosed to all staff and accessible for all staff at all times. Confidential aspects of the remuneration of single staff members are not subject to internal transparency.

70. Staff should be informed about the characteristics of their variable remuneration, as well as the process and criteria that will be used to assess the impact of their professional activities on the risk profile of the investment firm and their variable remuneration. In particular, the appraisal process with regard to the individual's performance should be properly documented and should be transparent to the staff concerned.

3. Remuneration policies and group context

71. In accordance with Article 25 of Directive (EU) 2019/2034, investment firms must, without prejudice to the derogations foreseen under Article 32(4) of Directive (EU) 2019/2034, comply with all requirements of Articles 26, 30, 31, 32 and 33 of that Directive. This includes the applicable Regulatory Technical Standards regarding remuneration. The requirements and their specifications within these guidelines apply on an individual basis and, where applicable, on a consolidated basis as referred to in Article 7 of Regulation (EU) 2019/2033.

72. At the consolidated level, the Union parent undertaking and competent authorities should ensure that a remuneration policy is implemented and complied with for all staff, including all identified staff, in all investment firms and other entities within the scope of prudential consolidation and all branches. The remuneration policy should be gender neutral. Specific remuneration requirements of subsidiaries should be taken into account.

73. Regarding investment firms and entities within a group located in more than one Member State, the group-wide remuneration policy should specify how its implementation should deal

with differences between national implementations of the remuneration requirements of Directive (EU) 2019/2034.

74. When applying the requirements on a consolidated basis, the remuneration requirements applicable in the Member State where the Union parent undertaking is located apply, including to identified staff who have a material impact on the group's risk profile, even if implementation of the requirements within Articles 30 and 32 of Directive (EU) 2019/2034 by the Member State where the Union parent undertaking is located is stricter.

75. Staff seconded from a parent undertaking in a third country to an EU subsidiary that is an investment firm or a branch who, were they employed directly by the EU investment firm or branch, would fall into the scope of identified staff of that EU investment firm or branch, are identified staff. Such seconded staff should be subject to the remuneration provisions within Directive (EU) 2019/2034 as they are implemented in the Member State where the EU investment firm or branch is established and to applicable Regulatory Technical Standards. For the purposes of short-term secondments, for example where a person is only residing in a Member State for a few weeks to carry out project work, that person should be subject to such provisions only if the person would be identifiable under the RTS on identified staff, taking into account the remuneration awarded for the relevant time period and the role and responsibilities during the secondment.

76. Short-term contracts or secondments must not be used as a means of circumventing the remuneration requirements of Directive (EU) 2019/2034 and any related standards or guidelines.

77. The remuneration requirements of Directive (EU) 2019/2034 and the provisions of these guidelines apply to investment firms in Member States independent of the fact that they may be subsidiaries of a parent investment firm or an institution in a third country. Where an EU subsidiary of an parent investment firm in a third country is a Union parent undertaking, the scope of prudential consolidation does not include the level of the parent investment firm located in a third country and other direct subsidiaries of that parent investment firm. The Union parent undertaking should ensure that the group-wide remuneration policy of the parent investment firm in a third country is taken into consideration within its own remuneration policies as far as this is not contrary to the requirements set out under relevant EU or national law, including these guidelines.

4 Proportionality

78. The proportionality principle as set out under Article 26(3) of Directive (EU) 2019/2034 aims to match remuneration policies and practices consistently with the individual risk profile, risk appetite and strategy of an investment firm, so that the objectives of the remuneration requirements are effectively achieved.

79. When applying the remuneration requirements and the provisions of these guidelines in a proportionate manner, investment firms and competent authorities should consider the nature, scale and complexity and the risks inherent in the business model and the activities of the investment firm.

80. The obligation to have sound and effective remuneration policies and practices applies to all investment firms with respect to all staff, regardless of the investment firms' different characteristics.

81. When assessing what is proportionate and in determining the required level of sophistication of the remuneration policies and risk measurement approaches, investment firms and competent authorities should take into consideration the combination of qualitative and quantitative aspects of all the criteria above. For instance, a business activity may well have a small scale but could still include complex activities and risk profiles because of the nature of its activities or the complexity of its products.

82. Where investment firms are authorised to provide the services and activities listed in point (2), (3), (4), (6) and (7) of Section A of Annex 1 to Directive 2014/65/EC, as a general principle a higher level of sophistication should be expected, in particular, if the investment firm is authorised to hold clients' money or assets.

83. For the above purposes, investment firms and competent authorities should take into account at least the following criteria:

    a. the on and off-balance-sheet assets of the investment firm and whether the investment firm meets the criteria and the thresholds set out in paragraphs 4 of Article 32 of Directive (EU) 2019/2034;

    b. if the investment firm is authorised to hold clients' money or assets;

    c. the type of authorised activities and services (e.g. Sections A and B of Annex I to Directive 2014/65/EU) and other services (e.g. clearing services) performed by the investment firm;

    d. the amount of assets under management;

    e. the assets safeguarded and administered;

    f. the volume of client orders handled;

    g. the volume of daily trading flow;

    h. the geographical presence of the investment firm and the size of the operations in each jurisdiction, including in third countries;

    i. the legal form and the available equity and debt instruments;

j. the methods used to determine the capital requirements;

k. whether the investment firm is part of a group and, if so, the proportionality assessment done for the group and the characteristics of the group to which the investment firm belongs;

l. the underlying business strategy;

m. the structure of the business activities and the time horizon, measurability and predictability of the risks of the business activities;

n. the funding structure of the investment firm;

o. the internal organisation of the investment firm, including the level of variable remuneration that can be paid to identified staff;

p. the main sources and structure of profits and losses of the investment firm;

q. the type of clients (e.g. retail, corporate, small businesses, public entity);

r. the complexity of financial instruments or contracts;

s. the outsourced functions and distribution channels;

t. the existing information technology (IT) systems, including continuity systems and outsourcing functions in this area.

84. Before remuneration requirements and the provisions set out in these guidelines are applied in a proportionate way, the identification of staff, based on the criteria provided in Article 30(1) of Directive (EU) 2019/2034 and the Commission Delegated Regulation mandated under Article 30(4) of that Directive (RTS on identified staff) and additional internal criteria, should be performed[17].

85. When implementing specific remuneration policies for different categories of identified staff in line with sections 3 and 4 of these guidelines, the application of proportionality should take into account the impact on the risk profile of the investment firm or the assets it manages of that category of identified staff.

86. Competent authorities should ensure that investment firms comply with the remuneration requirements and the provisions set out in these guidelines in a manner that provides for a level playing field among different investment firms.

[17] Please refer to guidelines for the identification process outlined in section 5 of these guidelines.

Waivers of the variable remuneration pay-out process

87. Without prejudice to the implementation of Article 32(4) of Directive 2019/2034/EU by Member States, an investment firm with total assets under the threshold defined in national law may not apply the requirements to defer variable remuneration and to pay it out in instruments as set out in points (j), (l) of Article 32(1) and the third subparagraph of Article 32(3) of Directive (EU)2019/2034.

88. When establishing the amount of the annual variable remuneration paid to a staff member and the effective ratio between the variable and fixed annual remuneration for the purposes of point (b) of Article 32(4) of Directive (EU) 2019/2034, i.e. the application of waivers to the requirement to defer and pay out in instruments the variable remuneration to individual staff members, investment firms should take into account the amounts specified in point (a) and (b) and apply the further conditions in points (c) to (h):

    a. the annual variable remuneration awarded for the performance period that equals the financial year for which it is determined if the waiver can be applied and all performance periods that ended in this financial year, independent of the length of the underlying performance periods that have ended in this financial year, e.g. it should include the full amount of variable remuneration based on revolving and non-revolving multi-year accrual periods and retention bonuses for periods longer than one year where the underlying period ended in the given financial year;

    b. the annual fixed remuneration awarded for the preceding performance year; investment firms may not take into account other awards that are considered fixed remuneration under paragraphs 127 and 128;

    c. the variable remuneration awarded for the preceding performance year, independent on how the remuneration is paid, i.e. cash, instruments or other forms of variable remuneration;

    d. the variable remuneration should consist of all forms of variable remuneration awarded, including performance-based variable remuneration, amounts paid as guaranteed variable remuneration, retention bonuses, severance payments or discretionary pension benefits;

    e. the amount of variable remuneration awarded for performance periods that are longer than one year, e.g. based on long-term incentive plans or multi-year accrual periods, taking into account the full amount for the performance year in which the performance periods end;

    f. the full amount of variable remuneration awarded within the performance year as guaranteed variable remuneration, retention bonuses, severance payments and discretionary pension benefits;

g. the amounts should be based on the definition for fixed and variable remuneration within these guidelines and should be calculated based on the gross remuneration awarded;

h. where the amount is determined on an individual basis, the remuneration awarded by the investment firm should be taken into account; where the amount is determined on a consolidated basis, all remuneration awarded within the scope of prudential consolidation should be taken into account; and

i. where the remuneration is paid in a currency other than EUR, the amounts should be converted into EUR using the exchange rate published by the Commission for financial programming and the budget for the last month of the investment firm's financial year.[18]

89. When calculating the average of the value of the assets for the four-year period immediately preceding the current financial year for the purpose of point (a) of Article 32 (4) of Directive (EU) 2019/2034, investment firms should use the simple average of this value at the end of the four preceding financial years. Where the accounts are kept in a currency other than EUR, the amounts should be converted into EUR using the exchange rate published by the Commission for financial programming and the budget for the last month of each financial year.

90. Where national law empowers competent authorities to set the thresholds under point (a) of Article 32(4) of Directive (EU) 2019/2034 for individual investment firms, competent authorities should, when lowering or increasing the thresholds, take into account the investment firms' nature, scope and complexity of its activities, its internal organisation or, if applicable, the characteristics of the group to which it belongs, and also take into account the proportionality criteria set out within these guidelines. The same applies with regard to reductions of the thresholds set in points (c), (d) and (e) Article 32(5) and Article 32(6).

91. Where national law empowers competent authorities to set the thresholds under Article 32(7) of Directive (EU) 2019/2034 for individual staff members, competent authorities should, when lowering the threshold, take into account the criteria within this Article and the impact of the staff members' professional activities on the risk profile of the investment firm and the assets it manages compared to other identified staff. For example, where a more material impact on the risk profile exists, it might be appropriate to require deferral and pay-out in instruments to be applied.

5. The identification process

92. It is the responsibility of investment firms to identify the members of staff whose professional activities have a material impact on the risk profile of the investment firm or the assets it manages (identified staff). All investment firms should conduct annually a self-assessment in order to identify all staff whose professional activities have or may have a material impact on

[18] The exchange rates can be found on the website of the European Commission under: http://ec.europa.eu/budget/contracts_grants/info_contracts/inforeuro/inforeuro_en.cfm

the risk profile of the investment firm or the assets it manages. The identification process should be part of the overall remuneration policy of the investment firm.

93. The self-assessment should be based on the qualitative and quantitative criteria set out in the RTS on identified staff and, where needed, to ensure the complete identification of all staff whose professional activities have a material impact on the risk profile of the investment firm or the assets it manages, additional criteria set forth by the investment firm that reflect the levels of risk of different activities within the investment firm and the impact of staff members on the risk profile.

94. When applying quantitative criteria based on staff members' remuneration, the fixed remuneration awarded for the preceding financial year and the variable remuneration awarded to staff in or for the preceding financial year should be taken into account. The variable remuneration awarded in the preceding financial year is the variable remuneration awarded in the preceding financial year with reference to previous performance. Investment firms should define the applicable method in their remuneration policy. When applying quantitative criteria based on staff's remuneration, investment firms should take into account all monetary and non-monetary fixed and variable remuneration components awarded for professional services. Routine remuneration packages that are not accounted for on an individual level should be taken into account based on the overall sum broken down by objective criteria to the individual staff member.

95. When applying quantitative criteria defined in EUR, investment firms which award remuneration in a currency other than the euro should convert the applicable thresholds using either the internal exchange rate used for the consolidation of the accounts or the exchange rate used by the Commission for financial programming and the budget for the month where the remuneration was awarded or the exchange rate for the last month of the investment firm's financial year. The investment firm should document the applicable method to determine the exchange rate in their remuneration policy.

96. The self-assessment should be clear, consistent, properly documented and periodically updated during the year at least with regard to qualitative criteria within the RTS on identified staff and, where appropriate, in addition based on investment firms' criteria. Investment firms should ensure that staff who fall or are likely to fall under the criteria in Article 3 of the RTS on identified staff for a period of at least three months in a financial year are treated as identified staff.

97. The following information should at least be included in the documentation of the self-assessment done regarding the identification of staff:

    a. the rationale underlying the self-assessment and the scope of its application;

    b. the approach used to assess the risks emerging from the investment firm's business strategy and activities, including in different geographical locations;

c. how persons working in investment firms and other entities within the scope of consolidation, subsidiaries and branches, including such located in third countries, are assessed;

d. the role and responsibilities of the different corporate bodies and internal functions involved in the design, oversight, review and application of the self-assessment process; and

e. the identification outcome.

98. Investment firms should keep records of the identification process and its results and should be able to demonstrate to their competent supervisory authority how staff have been identified according to both the qualitative and quantitative criteria provided for within the RTS on identified staff and any additional criteria used by the investment firms.

99. The documentation of the self-assessment should at least include the number of identified staff, including the number of staff identified for the first time, the job responsibilities and activities, the names or another unique identifier and the allocation within the investment firm of the identified staff to business areas and a comparison with the results of the previous year's self-assessment.

100. The documentation should also include staff members who have been identified under quantitative criteria, but whose professional activities are assessed as not having a material impact on the risk profile of the investment firm or the assets it manages, in accordance with RTS on identified staff. Investment firms should maintain the documentation for an appropriate time period to enable the review by the competent authorities.

5.1 Prior approval of exclusions

101. Where the investment firm determines in accordance with the RTS on identified staff that the professional activities of the staff member do not have a material impact on the investment firm or the assets it manages and applies for a prior approval, the following should apply:

a. the management body should decide based on the performed analysis within the annual identification process if staff have in fact no material impact on the risk profile of the investment firm or the assets it manages and inform the supervisory function of the decision taken. The supervisory function or the remuneration committee when it is established should review the criteria and process under which the decisions are taken and approve the exemptions made;[19]

b. any application for prior approval should be made without delay, but at the latest within six months after the end of the preceding financial year. The competent authority should assess the application and approve or reject the application, to the extent possible, within a three-month period after receiving the complete documentation;

[19] Please refer to paragraph 103 with regard to the approval of exemptions to the remuneration policy.

c. where the staff member was awarded total remuneration of EUR 1,000,000 or more in the preceding financial year, the competent authority should immediately inform the European Banking Authority about the application received and provide its initial assessment. On request, the competent authority should immediately submit all information received by the investment firm to the EBA. The EBA will liaise with the competent authority to ensure that such exclusions are granted in a consistent way before the decision regarding the approval or rejection of the application is taken by the competent authority.

102. The prior approval regarding exclusions of staff identified in relation to the quantitative criteria should be granted only for a limited time period. The request for prior approval under the RTS on identified staff should be made each year. With respect to staff for whom a decision on the application is taken for the first time, the prior approval should only concern the financial year in which the prior approval was requested and the following financial year. For staff for whom the exclusion has already been approved for the ongoing financial year, the prior approval should only concern the following financial year.

103. Where identified staff would be excluded in subsidiaries which are not themselves subject to Directive (EU) 2019/2034, the competent authority is the competent authority of the parent investment firm. For branches of investment firms where the head office is located in a third country, the competent authority is the competent authority responsible for the supervision of investment firms in the Member State where the branch is located.

104. Requests for prior approval should include all names or another unique identifier for identified staff for whom an exclusion should apply, the percentage of the business unit's contribution to the investment firm's total own funds requirement in which the staff member is active and the analysis of the impact of staff on the investment firm's risk profile for each identified staff member. Where identified staff are active in the same business unit and have the same function, a joint assessment should be made.

5.2 Governance of the identification process

105. The management body has the ultimate responsibility for the identification process and the respective policy. The management body in its supervisory function should:

a. approve the identification process policy as part of the remuneration policy;

b. be involved in the design of the self-assessment;

c. ensure that the assessment for the identification of staff is properly made in accordance with Directive (EU) 2019/2034, the RTS on identified staff and these guidelines;

d. oversee the identification process on an ongoing basis;

e. approve any material exemptions from or changes to the adopted policy and carefully consider and monitor their effect;

f. approve or oversee any exclusion of staff in accordance with the RTS on identified staff where the investment firm deems that the quantitative criteria defined in the RTS on identified staff are not met by the staff, as they, in fact, do not have a material impact on the risk profile of the investment firm or the assets it manages;

g. periodically review the approved policy and, if needed, amend it.

106. Where a remuneration committee is established, it should be actively involved in the identification process in line with its responsibilities for the preparation of decisions regarding remuneration. Where no remuneration committee is established, the non-executive and where possible the independent members of the management body in its supervisory function should execute the respective tasks.

107. The compliance function, the risk management function or the staff entrusted with the risk management procedures, the business support functions (e.g. legal, human resources) and the relevant committees of the management body (i.e. risk, nomination and audit committees) should be involved in the identification process in accordance with their respective role and also on an ongoing basis. In particular, where a risk committee is established, it should be involved in the identification process without prejudice to the tasks of the remuneration committee. Investment firms should ensure a proper exchange of information among all internal bodies and functions involved in the identification process. The identification process and its result should be subject to an independent internal or external review.

5.3 Identification process on individual and consolidated level

108. When identifying the categories of staff under Article 30(1) of Directive (EU) 2019/2034, investment firms should apply the qualitative and quantitative identification criteria included RTS on identified staff and those additionally set by the investment firms both, on an individual basis, using the figures and considering the situation of the individual investment firm, and in addition on a consolidated basis. On a consolidated basis, the Union parent undertaking should apply the criteria using the consolidated figures and considering the consolidated situation and the impact on the investment firms' risk profile on a consolidated basis.

109. When applying qualitative identification criteria at consolidated level, staff members in a subsidiary are only captured if they are responsible for the functions referred to in these criteria on a consolidated basis. For example, a staff member in a subsidiary who is a member of the management body of such subsidiary should be captured by the criterion 'the staff member is a member of the management body in its management function' only if he or she is also a member of the management body of the EU parent investment firm.

110. When applying quantitative identification criteria on a consolidated basis, investment firms should take into account all remuneration awarded to a staff member within the full scope of prudential consolidation.

111. When applying qualitative identification criteria, investment firms should identify the staff responsible for the function named in the qualitative criteria; the main criterion for the identification is not the name of the function but the authority and responsibility conferred on the function.

5.4 Role of the Union parent undertaking

112. The Union parent undertaking should ensure the overall consistency of the group remuneration policies, including the identification processes and the correct implementation on a consolidated and solo basis.

5.5 Role of subsidiaries and branches

113. Investment firms that are subsidiaries of a Union parent undertaking should implement within their remuneration policy the policy issued by the consolidating Union parent undertaking and the process for the identification of staff.

114. All subsidiaries should actively participate in the identification process carried out by the consolidating Union parent undertaking. In particular, each subsidiary in the scope of prudential consolidation, including those not themselves subject to Directive (EU) 2019/2034, should provide the Union parent undertaking with all information necessary to properly identify all staff who have a material impact on the risk profile of the investment firm or the assets it manages on a consolidated basis.

115. Subsidiaries that are not themselves subject to Directive (EU) 2019/2034 are not required to perform an identification process on the solo level, unless they are required to do so under sector-specific remuneration requirements. For those subsidiaries that are not subject to the Directive or other specific remuneration requirements, the assessment should be performed by the Union parent undertaking on the consolidated basis, based on information provided by the subsidiary. Investment firms falling within the scope of Directive (EU) 2019/2034 should conduct their own self-assessment for the identification of staff on the solo level. Investment firms which are included in an identification process on a consolidated basis may delegate the practical application of the identification process on a solo level to the Union parent undertaking.

116. Branches in a Member State of investment firms having their head office in a third country and investment firms in a Member State which are subsidiaries of parent investment firms in third countries should conduct the identification process and inform their parent investment firm of its results. Investment firms in a Member State should also include their subsidiaries that fall in the scope of prudential consolidation and branches located in third countries in their assessment. Investment firms should be aware that branches form a non-independent part of the investment firm.

117. For third country branches located in a Member State, the criteria for the identification should be applied in the same way to the functions, business activities and staff located in a Member State as they would be for an investment firm on an individual level.

6. Capital base

118. Investment firms and competent authorities should ensure that the award, pay-out and vesting of variable remuneration, including the application of malus and clawback arrangements under the investment firms' remuneration policy, is not detrimental to the investments firms' ability to ensure a sound capital base.

119. When assessing if the capital base is sound, the investment firm should take into account its overall own funds, its composition and in particular the Common Equity Tier 1 capital and its own funds' requirements. The requirement to maintain a sound capital base also applies on a consolidated basis. Additionally, competent authorities should take into account the results of their supervisory reviews.

120. Investment firms should include the impact of variable remuneration - both upfront and deferred amounts - in their capital and liquidity planning and in their overall internal capital adequacy assessment process.

121. The total variable remuneration awarded by an investment firm must not limit the ability of the investment firm to maintain or restore a sound capital base in the long term and should consider the interests of shareholders and owners, investors and other stakeholders. Variable remuneration should not be awarded or paid out when the effect would be that the capital base of the investment firm would no longer be sound. The investment firm should consider these requirements, the results from the internal capital adequacy assessment process, its multi-year capital planning and recommendations on distributions by competent authorities and European Supervisory Authorities, when determining:

a. the overall pool of variable remuneration that can be awarded for that year; and

b. the amount of variable remuneration that will be paid out or will be vesting in that year.

122. Investment firms which do not have a sound capital base or where the soundness of the capital base is at risk should take the following measures with regard to variable remuneration:

a. reduce the variable bonus pool, including the possibility to reduce it down to zero;

b. apply the necessary performance adjustment measures, in particular malus;

c. use the net profit of the investment firm for that year and potentially for subsequent years to strengthen the capital base. The investment firm should not compensate for any reduction of the variable compensation made in order to ensure a sound capital basis in

later years or by other payments, vehicles or methods which lead to a circumvention of this provision.

123. Competent authorities should intervene where the awarding of variable remuneration is detrimental to the maintenance of a sound capital base by requiring the investment firm to reduce or apply a cap to the overall pool of variable remuneration determined until the capital adequacy situation improves; and if necessary to apply performance adjustment measures, in particular malus, and require investment firms to use net profits to strengthen own funds.

Title II - Structure of remuneration

7. Categories of remuneration

124. Under Directive (EU) 2019/2034, remuneration is either fixed or variable remuneration; there is no third category of remuneration. Without prejudice to the national implementation of waivers under paragraphs (4) to (7) of Article 32 of Directive (EU) 2019/2034, where remuneration is variable and is paid to identified staff, all requirements of Article 32 of Directive (EU) 2019/2034 have also to be met in addition to the general requirements contained in Articles 26 and 30 thereof. For that purpose, investment firms should allocate in line with these guidelines the components of remuneration to either fixed or variable remuneration and their remuneration policies should set out clear, objective, predetermined and transparent criteria to assign all remuneration components to either the fixed or variable categories in line with these guidelines.

125. Where the clear allocation of a component to the fixed remuneration is not possible based on the criteria provided in these guidelines, it should be considered as variable remuneration.

126. Remuneration is fixed where the conditions for its award and its amount:

a. are based on predetermined criteria;

b. are non-discretionary reflecting the level of professional experience and seniority of staff;

c. are transparent with respect to the individual amount awarded to the individual staff member;

d. are permanent, i.e. maintained over a period tied to the specific role and organisational responsibilities;

e. are non-revocable; the permanent amount is only changed via collective bargaining or following renegotiation in line with national criteria on wage setting;

f. cannot be reduced, suspended or cancelled by the investment firm;

g. do not provide incentives for risk assumption; and

h. do not depend on performance.

127. Remuneration components that are either part of a general investment firm-wide policy where they meet the conditions listed in paragraph 128 or payments mandatory under national law, are considered as fixed remuneration. This includes payments which form part of routine employment packages as defined in these guidelines.

128. The following remuneration components should also be considered as fixed, where all similar situations are treated in a consistent way:

a. remuneration paid to expatriate staff considering the cost of living and tax rates in a different country;

b. allowances used to increase the basic fixed salary in situations where staff work abroad and receive less remuneration than would be paid on the local employment market for a comparable position where all of the following specific conditions are met:

i. the allowance is paid on a non-discriminatory basis to all staff in a similar situation;

ii. the allowance is awarded because staff work temporarily abroad or in a different position with a remuneration level requiring adjustment to reflect pay levels in the relevant market;

iii. the level of additional payments is based on predetermined criteria;

iv. the duration of the allowance is tied to the duration of the situation referred to above.

8. Particular cases of remuneration components

8.1 Allowances

129. The variable and fixed remuneration of investment firms may consist of different components, including additional or ancillary payments or benefits. Investment firms should analyse allowances[20] and allocate them to the variable or fixed component of remuneration. The allocation should be based on the criteria in section 7.

130. In particular where allowances are considered as fixed remuneration, but show any of the following features, the investment firm should duly document the results of the assessments made under section 7:

[20] The label may differ according to the investment firm: 'role-based pay, staff allowance, adjustable role allowance, fixed pay allowance', etc.

a. they are paid only to identified staff members[21];

b. they are limited to cases where the ratio between the variable and the fixed components of remuneration would otherwise exceed the ratio set within the remuneration policy;

c. the allowances are linked to indicators that could possibly be understood as proxies for performance. In that case the investment firm should be able to demonstrate that these indicators are not linked to the performance of the investment firm, e.g. by analysing the correlation with the performance indicators used.

131. Where allowances are based on the role, function or organisational responsibility of staff, in order to be correctly mapped to the fixed component of remuneration, they should meet the criteria set out in paragraph 128 taking into account all of the following particulars:

a. the allowance is tied to a role or organisational responsibility and awarded as long as no material changes happen regarding the responsibilities and authorities of the role so that in fact the staff would have a different role or organisational responsibility;

b. the amount does not depend on any factors other than fulfilling a certain role or having a certain organisational responsibility and the criteria in paragraph 14;

c. any other staff member fulfilling the same role or having the same organisational responsibility and who is in a comparable situation would be entitled to a comparable allowance.

132. Competent authorities should ensure that allowances are not a vehicle or method that facilitates the non-compliance of investment firms with Directive (EU) 2019/2034.

8.2 Variable remuneration based on future performance

133. When the award of variable remuneration, including long term incentive plans (LTIPs), is based on past performance of at least one year, but also depends on future performance conditions, the following should apply:

a. investment firms should clearly set out to staff the additional performance conditions that have to be met after the award for the variable remuneration to vest;

b. investment firms should assess before the vesting of variable remuneration that the conditions for its vesting have been met;

c. the additional forward-looking performance conditions should be set for a predefined performance period of at least one year;

[21] Being an identified staff member should not be considered as a role or function.

d. when the additional forward looking performance conditions have not been met, up to 100% of the variable remuneration awarded under those conditions should be subject to malus arrangements;

e. the deferral period should end at the earliest one year after the last performance condition has been assessed; all other provisions regarding the deferral of variable remuneration for identified staff set out in section 15 apply in the same way as to variable remuneration that is exclusively based on performance previous to its award;

f. for the calculation of the ratio between the variable and the fixed component of the total remuneration, the total amount of the variable remuneration awarded should be taken into account in the financial year for which the variable remuneration, including LTIPs, was awarded. This should also apply when the past performance was assessed in a multi-year accrual period.

134. Where a prospective remuneration plan for variable remuneration, including LTIPs, is exclusively based on future performance conditions (e.g. where new staff receive an LTIP at the beginning of the first year of employment), the amount should be considered as awarded after the performance conditions have been met, and otherwise no award should be made. Awarded amounts should be taken into account for the calculation of the ratio between the variable and the fixed component of the total remuneration in the financial year prior to their award. Where a specific number of instruments are awarded, they should exceptionally be valued for the purpose of the calculation of the ratio between the variable and the fixed component of the total remuneration with the market price or fair value determined at the time the prospective remuneration plan for variable remuneration was granted. Points (a) to (c) of paragraph 134 should apply. All other requirements apply in the same way as to variable remuneration, e.g. the deferral period starts after the award of the variable remuneration.

8.3 Dividends and interest payments

135. Dividends paid on vested shares or equivalent ownership interests that staff receive as shareholders or owners of an investment firm are not part of remuneration for the purpose of these guidelines. The same applies to interest paid to staff on other instruments awarded after they have vested.

8.4 Retention bonuses

136. Investment firms should be able to substantiate their legitimate interest in awarding retention bonuses to retain an identified staff member. For example, retention bonuses may be used under restructurings, in wind-down or after a change of control or to ensure the finalisation of major projects within an investment firm. Investment firms should document the event or justification that made it necessary to award a retention bonus and the time period,

including the start and the end date, for which the reason is assumed to exist. Investment firms should define the retention conditions and applicable performance conditions. Investment firms should specify a retention period and a date or event after which it determines whether the retention and performance conditions have been met.

137. As a general principle, investment firms should not award multiple retention bonuses to a staff member; in exceptional cases and where duly justified, more than one retention bonus may be paid to a staff member, but at different moments in time and under the conditions specified in this section with regard to each retention bonus. The retention bonuses should only be awarded after the retention conditions and applicable performance conditions have been met. Moreover, the retention bonus should only be awarded if no reasons exist that lead to a situation where the retention bonus should not be awarded, e.g. material compliance breaches, misconduct or other failures of that staff member.

138. A retention bonus should be in accordance with the requirements to maintain a sound capital base under Article 31 and Article 32(1)(d) of Directive (EU) 2034/2019 and the respective supervisory powers under Article 39(2)(g) of Directive (EU) 2034/2019 that could lead to a situation where the retention bonus might need to be reduced, possibly even down to zero.

139. When assessing and considering whether the award of a retention bonus to identified staff is appropriate, investment firms and competent authorities may take into account at least the following:

a. the concerns that lead to the risk that certain staff may choose to leave the investment firm;

b. the reasons why the retention of those staff is crucial for the investment firm;

c. the consequence if the staff member concerned leaves the investment firm;

d. whether the amount of the awarded retention bonus is necessary and proportionate to retain the targeted staff member.

140. A retention bonus should be based on specific conditions that differ from the performance conditions applied to other parts of the variable remuneration and include a retention condition and specific performance conditions. The specific conditions for a retention bonus should lead to the retention objective (i.e., retention of staff in the investment firm for a predefined period of time or until a certain event). The specific performance conditions should include conditions that are related to the legitimate interest for which the staff member should be retained, the conduct of staff and be compatible with the provisions in paragraph 138. Retention bonuses should not lead to a situation where the total variable remuneration, consisting of performance-related variable remuneration and retention bonus, of the staff member is no longer linked to the performance of the individual, the business unit concerned and the overall results of the investment firm as required under Articles 30(j)(ii) and 32(1)(a) of Directive (EU) 2034/2019.

141. Retention bonuses should not be awarded to merely compensate for performance-related remuneration not paid due to insufficient performance or the investment firm's financial situation.

142. Investment firms should set the retention period as the point in time of the event or as the period between the start date and the end date of the event when the retention condition should be met. The retention bonuses should be awarded after the retention period ends. No pro rata awards should be made during the retention period.

143. Retention bonuses are variable remuneration and therefore if awarded to identified staff, must comply with the requirements on variable remuneration under Article 32 of IFD, including the internally set maximum ratio between the variable and fixed remuneration, the ex post risk alignment, payment in instruments, deferral, retention, malus and clawback.

144. Independent of the fact that the retention bonus will be awarded only after the end of the retention period, the retention bonus should be taken into account in the calculation of the ratio between the variable and the fixed part of remuneration following one of the methods specified below:

a. the retention bonus is split into annual amounts for each year of the retention period calculated on a linear pro rata basis. Where the exact length of the retention period is not known upfront, the investment firm should set and duly document a period considering the situation and measures taken that justify the payment of a retention bonus. The calculation of the ratio should be based on the period set, or

b. the full amount of the retention bonus is considered in the year when the retention condition is met.

8.5 Discretionary pension benefits

145. Discretionary pension benefits are a form of variable remuneration. Where the terms of the company's pension scheme include pension benefits that are not based on performance and are consistently granted to a category of staff, such pension benefits should not be considered discretionary, but should be considered as part of routine employment packages in line with the section of these guidelines on definitions. Discretionary pension benefits are not severance payments, even if the employee decides to retire early.

146. The investment firm should ensure that where a staff member leaves the investment firm or retires, discretionary pension benefits are not paid without the consideration of the economic situation of the investment firm or risks that have been taken by the staff member which can affect the investment firm in the long term.

147. The full amount of discretionary pension benefits must be awarded, in accordance with Article 32(3) of Directive (EU) 2019/2034 and subject to the derogation under Article 32(4) of

this Directive, in instruments referred to in point (j) of this Article or, where approved by competent authorities, within the alternative arrangements under Article 32(1)(k) and:

a. where an identified staff member leaves the investment firm before retirement, the investment firm must hold the full amount of discretionary pension benefits at least for a period of five years without the application of pro rata vesting;

b. where identified staff member reaches retirement, a five-year retention period must be applied to the full amount paid.

148. Investment firms should ensure that malus and clawback arrangements are applied in the same way to discretionary pension benefits as to other components of variable remuneration.

9. Exceptional remuneration components

9.1 Guaranteed variable remuneration

149. Guaranteed variable remuneration can take several forms such as a 'guaranteed bonus', 'welcome bonus', 'sign-on bonus', 'minimum bonus' etc., and can be awarded either in cash or in instruments.

150. When awarding guaranteed variable remuneration in accordance with Article 32(1)(e) of Directive (EU) 2019/2034 when hiring new staff, investment firms are not permitted to guarantee variable remuneration for longer than the first year of employment. Guaranteed variable remuneration is exceptional and can only occur where the investment firm has a strong capital base in line with these guidelines.

151. Investment firms should only award once to the same single staff member guaranteed variable remuneration. This requirement should also apply at a consolidated level and includes situations where staff receive a new contract from the same investment firm or another firm within the scope of consolidation.

152. As part of the arrangements guaranteeing this part of variable remuneration, investment firms may decide to not apply the requirements on malus and clawback arrangements to guaranteed variable remuneration. Investment firms may pay out the full amount in non-deferred cash.

9.2 Compensation or buyout from previous employment contract

153. The compensation for the buyout of a previous contract should be awarded only when the conditions defined in section 9.1 of these guidelines are met.

154. Remuneration should be considered as being granted as compensation or for the buyout of a previous contract where the deferred variable remuneration of the staff member was reduced or revoked by the previous employer because of the termination of the contract or

where the staff member has to reimburse received payments (e.g. as part of an educational expense coverage agreement). For remuneration packages relating to compensation or buyout from contracts in previous employment, all requirements for variable remuneration and the provisions within these guidelines apply, including deferral, retention, pay-out in instruments and clawback arrangements.

9.3 Severance and other payments after the end of a contract

9.3.1 Severance pay

155. Investment firms' remuneration policies should specify the possible use of severance payments, including the maximum amount or criteria for the determination of such amounts that can be awarded as severance pay to identified staff. When determining the maximum amounts of severance payments, investment firms should consider in particular the fixed components of the remuneration of staff. Investment firms should consider how they will apply the ratio set between the variable and fixed remuneration to severance payments.

156. Investment firms should have a framework in which severance pay is determined and approved in the context of the early termination of a contract by the investment firm, including a clear allocation of the responsibilities and decision-making powers and the procedural involvement of the control functions.

157. Severance payments should not provide for a disproportionate reward, but for an appropriate compensation of the staff member in cases of early termination of the contract. In accordance with Article 32(1)(f) of Directive (EU) 2019/2034 severance payments must reflect performance achieved over time and must not reward failure or misconduct.

158. Severance pay should not be awarded where there is an obvious failure which allows for the immediate cancellation of the contract or the dismissal of staff.

159. Severance pay should not be awarded where a staff member resigns voluntarily in order to take up a position in a different legal entity, unless a severance payment is required by national labour law.

160. Additional payments in the context of the regular end of a contractual period or appointment as member of the management body, e.g. awarded discretionary pension benefit, should not be treated as severance payments, but as normal variable remuneration that is for identified staff subject to all specific requirements for variable remuneration.

161. Severance payments include additional payments on top of the regular remuneration in the following specific situations:

   a. redundancy remuneration for loss of office in case of an early termination of the contract by the investment firm or its subsidiary;

b. remuneration awarded for a limited time period that is agreed to introduce a cooling-off period after the termination of the contract and is subject to a non-competition clause in the contract;

c. the investment firm terminates the contracts of staff because of a failure of the investment firm or early intervention measures;

d. the investment firm wants to terminate the contract following a material reduction of the investment firm's activities in which the staff member was active or where business areas are acquired by other investment firms without the option for staff to stay employed in the acquiring investment firm;

e. the investment firm and a staff member agree on a settlement in case of an actual labour dispute that could otherwise realistically lead to an action in front of a court.

162. Where investment firms award severance pay, the investment firms should be able to demonstrate to the competent authority the reasons for the severance payment, the appropriateness of the amount awarded and the criteria used to determine the amount, including that it is linked to the performance achieved over time and that it does not reward failure or misconduct.

163. When determining the amount of severance payments to be made, the investment firm should take into account the performance achieved over time and assess where relevant the severity of any failure. Identified failures should be distinguished between failures of the investment firm and failures of the identified staff as follows:

a. failures of the investment firm should be considered when the total amount of the severance payments for staff is determined, taking into account the capital base of the investment firm; such severance payments should not be higher than the reduction of costs achieved by the early termination of contracts;

b. failures of identified staff should lead to a downward adjustment of the amount of severance pay which would otherwise be awarded when only the performance over time would be considered in the estimation of the severance pay, including the possibility for a reduction of the amount down to zero.

164. Failures of investment firms include the following situations:

a. where the opening of normal insolvency proceedings of the investment firm, as defined in Article 2(1)(47) of Directive 2014/59/EU, has been filed;

b. where significant losses lead to the situation that the investment firm no longer has a sound capital base and, following this, the business area is sold or the business activity is reduced.

165. Failures of identified staff should be assessed on a case-by-case basis, and include the following situations:

a. where a member of the management body is no longer considered as meeting appropriate standards of fitness and propriety;

b. where the identified staff member participated in or is responsible for conduct which resulted in significant losses for the investment firm, as defined in the investment firms' remuneration policy;

c. where an identified staff member acts contrary to internal rules, values or procedures based on intent or gross negligence.

166. Severance payments should be considered as variable remuneration and as a general principle therefore, if awarded to identified staff, all requirements under Article 32 of Directive (EU) 2019/2034 apply. However, severance payments should in the following circumstances not be taken into account for the purpose of the calculation of the ratio between variable and fixed remuneration set within the remuneration policy and for the application of deferral and the pay out in instruments:

a. severance payments mandatory under national labour law or mandatory following a decision of a court;

b. severance payments under (i) and (ii) where the investment firm is able to demonstrate the reasons and the appropriateness of the amount of the severance payment:

(i) severance payments calculated through an appropriate predefined generic formula (e.g. gardening leave) set within the remuneration policy in the cases referred to in paragraph 161;

(ii) severance payments corresponding to the additional amount due in application of a non-competition clause in the contract and paid out in future periods up to the amount of the fixed remuneration which would have been paid for the non-competition period, if staff were still employed.

c. severance payments under paragraph 161, not fulfilling the condition in point (i) of paragraph 166, where the investment firm has demonstrated to the competent authority the reasons and the appropriateness of the amount of the severance payment.

9.3.1 Other payments after the end of a contract

167. Regular remuneration payments related to the duration of a notice period should not be considered as severance payments. The payment of an appropriate fixed amount after the regular end of an employment contract (i.e. after coming to its regular end or being cancelled by staff in line with the applicable notice periods) and to compensate staff where the

investment firm restricts the taking up of an occupational activity, should not be subject to the requirements applicable to variable remuneration, where this is compatible with national law. Such payments should not be made to replace severance payments under paragraph 161.

168. Additional payments in the context of the regular end of a contractual period or of the appointment as member of the management body, e.g. awarded discretionary pension benefit should not be treated as severance payments. Where such components are variable remuneration and are paid to identified staff, they are subject to all specific requirements for variable remuneration and the provisions within these guidelines.

10 Prohibitions

10.1 Personal hedging

169. Where an appropriate remuneration policy is aligned with risks, it should be sufficiently effective and able to result in practice in a downward adjustment to the amount of variable remuneration awarded to staff and the application of malus and clawback arrangements.

170. Investment firms should ensure to the extent possible that identified staff members are not able to transfer the downside risks of variable remuneration to another party through hedging or certain types of insurance, e.g. by implementing policies for dealing in financial instruments and disclosure requirements.

171. Identified staff should be considered to have hedged the risk of a downward adjustment in remuneration if the identified staff member enters into a contract with a third party or the investment firm and either of the following conditions is met:

a. the contract requires the third party or the investment firm to make payments directly or indirectly to the identified staff member that are linked to or commensurate with the amounts by which the staff member’s variable remuneration has been reduced;

b. the identified staff member purchases or holds derivatives that are intended to hedge losses associated with financial instruments received as part of the variable remuneration.

172. Identified staff should be considered to have insured the risk of a downward adjustment where staff takes out an insurance contract with a stipulation to compensate them in the event of a downward adjustment in remuneration. This should in general not prevent taking out insurance to cover personal payments such as healthcare and mortgage instalments.

173. The requirement to not use personal hedging strategies or insurance to undermine the risk alignment effects embedded in their remuneration arrangements should apply to deferred and retained variable remuneration.

174. Investment firms should maintain effective arrangements to ensure that the identified staff member complies with the provisions of this section. At least a declaration of self-commitment by the identified staff member that he or she will refrain from concluding personal hedging strategies or insurances for the purpose of undermining the risk alignment effects is necessary. Where applicable, investment firms' human resources or internal control functions should perform at least spot-check inspections of the compliance with this declaration with regard to the internal custodianship accounts. Such random checks should at least include the internal custodianship accounts of identified staff. Notification to the investment firm of any custodial accounts outside the investment firm should also be made mandatory.

10.2 Circumvention

175. Investment firms should ensure that variable remuneration is not paid through vehicles or methods which aim at or effectively lead to non-compliance with remuneration requirements and the provisions of these guidelines for identified staff or, where such requirements are applied to all staff, with remuneration requirements for all staff. This includes arrangements between the investment firm and third parties where the staff member has a financial or personal interest.

176. 'Circumvention' is the non-compliance with remuneration requirements and takes place if an investment firm is actually not meeting the objective and purpose of requirements when considered together, while formally the investment firm complies with the wording of the single remuneration requirements.

177. Circumvention takes place in the following circumstances, among others:

a. where variable remuneration is considered as fixed remuneration in line with the wording of these guidelines, but not with its objectives;

b. where variable remuneration other than guaranteed variable remuneration is awarded or vests although, effectively:

   i. there has been no positive performance measured in line with Title IV of these guidelines by the staff member, business unit or investment firm;

   ii. there is no effective risk alignment (i.e. ex ante or ex post risk adjustment); or

   iii. the variable remuneration is not sustainable according to the investment firm´s financial situation;

c. where staff receive payments from the investment firm or an entity within the scope of consolidation which do not fall under the definition of remuneration, but are vehicles or methods of pay that contain an incentive for risk assumption or provide disproportionate returns on investments on instruments of the firm that are significantly different from conditions for other investors who would invest in such a vehicle;

d. where staff receive payments from the investment firm or an entity within the scope of consolidation which do not fall under the definition of remuneration, but are vehicles or methods to circumvent the remuneration requirements;

e. where fixed remuneration components are awarded as a fixed number of instruments and not as a fixed amount;

f. where staff are awarded remuneration in instruments or are able to buy instruments which are not priced at the market value or the fair value in the case of non-listed instruments and the additional value received is not taken into account in the variable remuneration;

g. where adjustments to fixed remuneration components are frequently negotiated and adjustments are in fact made to align the remuneration with the performance of staff;

h. where allowances are awarded at an excessive amount that is not justified for the underlying circumstances;

i. where remuneration is labelled as payment for early retirement and not taken into account as variable remuneration, where in fact the payment has the character of a severance pay, as it is made in the context of the early termination of the contract, or where in fact the staff member does not retire after such award is made or where the payments are not granted on a monthly basis;

j. any measures that would lead to a situation where in fact the remuneration policy would not any longer be gender neutral.

178. Investment firms should ensure that the method for measuring the performance has appropriate controls to ensure that the award criteria cannot be manipulated. Where such controls are not in place, the variable remuneration is not appropriately linked to performance and the remuneration policy is not appropriately implemented and any payment of variable remuneration can lead to a violation of regulatory requirements. Possible manipulations include, for instance, courtesy decisions in the bilateral performance measurement process, e.g. where no objective standards exist for the decision-making process regarding staff members' goal attainment.

179. Investment firms should not provide compensation for any reduction or restructuring of variable remuneration, e.g. made in the context of recovery and resolution measures or other exceptional government intervention, in later years or by other payments, vehicles or methods.

180. Investment firms should not create group structures or offshore entities or contracts with persons who act on behalf of the investment firm in order to manipulate the outcome of the identification process and to circumvent the application of the remuneration requirements and the provisions of these guidelines to staff to whom these requirements and provisions should otherwise apply.

181. Where short-term contracts (e.g. one year) are used and renewed on a regular basis by investment firms, competent authorities should review if such contracts form a vehicle or method of circumvention of the remuneration requirements of Directive (EU) 2019/2034, e.g. as they would in fact create variable remuneration, and take appropriate measures to ensure that investment firms comply with the requirements of Articles 30 and 32 of Directive (EU) 2019/2034.

182. Where remuneration is fixed remuneration in accordance with the guidelines in section 7, but is paid out in instruments, investment firms and competent authorities should consider if the instruments used turn the fixed component of remuneration into a variable component of remuneration, as a link to the performance of the investment firm is established. Investment firms should not use financial instruments as part of the fixed remuneration to circumvent variable remuneration requirements and the instruments used should not provide incentives for excessive risk taking.

Title III – Remuneration of specific functions

11. Remuneration of members of the management and supervisory function of the management body

183. The remuneration of the members of the management body in its management function (hereafter 'management function') should be consistent with their powers, tasks, expertise and responsibilities.

184. In order to properly address conflicts of interest and without prejudice to paragraphs 185 and 186, members of the supervisory function should be compensated for this role only with fixed remuneration. Incentive-based mechanisms based on the performance of the investment firm should be excluded. The reimbursement of costs to members of the supervisory function and the payment of a fixed amount for working hours or days, even if the time to be reimbursed is not predefined, are considered as fixed remuneration.

185. Where the supervisory function in exceptional cases is awarded variable remuneration, the variable remuneration and risk alignment should be strictly tailored to the assigned oversight, monitoring and control tasks, reflecting the individual's authorities and responsibilities and the achievement of objectives linked to their functions.

186. Where variable remuneration is awarded in instruments, appropriate measures should be taken to preserve the independence of judgement of those members of the management body, including the setting of retention periods until the end of the mandate.

12 Remuneration of control functions

187. The internal control functions should have sufficient resources, knowledge and experience to perform their tasks with regard to the investment firm's remuneration policy. The control

functions should cooperate actively and regularly with each other and other relevant functions and committees with regard to the remuneration policy and risks which may arise from remuneration policies.

188. The remuneration of staff in control functions should allow the investment firm to employ qualified and experienced personnel in these functions. The remuneration of control functions should be predominantly fixed to reflect the nature of their responsibilities.

189. The methods used for determining the variable remuneration of control functions, i.e. risk management, compliance and internal audit function, should not compromise staff's objectivity and independence.

Title IV – Remuneration policy, award and pay-out of variable remuneration for identified staff

13. Remuneration policy for identified staff

190. Investment firms must ensure that the remuneration policy for identified staff complies with all principles set out in Articles 30 and 32 and, where applicable, Article 31 of Directive (EU) 2019/2034 and is gender neutral.

191. The appropriate ratio between the variable and fixed remuneration components for identified staff should be set independent of any potential future ex post risk adjustments or fluctuation in the price of instruments.

192. Investment firms should implement, for different categories of identified staff, specific remuneration policies and risk alignment mechanisms as appropriate to ensure that the impact of the category of identified staff on the investment firm's risk profile is appropriately aligned with their remuneration.

193. Where investment firms consider paying out less than 100% of the fixed component of remuneration in cash, this decision should be well reasoned and approved as part of the remuneration policy.

194. Where an investment firm in the legal form of a stock corporation and in particular a listed investment firm applies a shareholding requirement to some categories of identified staff in order to achieve a better alignment of the incentives provided to staff with the risk profile of the investment firm in the long term, the amount should be clearly documented in the investment firm's policies. When a shareholding requirement is applied, staff should hold a certain number of shares or nominal amount of shares as long as they are employed in the same position or a position of equal or higher seniority.

13.1 Fully flexible policy on variable remuneration

195. Investment firms must have a fully flexible policy on variable remuneration for its staff, including identified staff, in accordance with Article 30(1)(k) of Directive (EU) 2019/2034. The amount of variable remuneration awarded should appropriately react to changes of the performance of the staff member, the business unit and the investment firm. The investment firm should specify how the variable remuneration reacts to performance changes and the performance levels. This should include performance levels where variable remuneration decreases down to zero. Unethical or non-compliant behaviour should lead to a significant reduction of the staff member's variable remuneration.

196. The amount of fixed remuneration must be sufficiently high in order to ensure that the reduction of the variable remuneration down to zero would be possible. Staff should not be dependent on the award of variable remuneration as this might otherwise create incentives for short-term-oriented excessive risk taking, including the mis-selling of products, where without such short-term risk taking the performance of the investment firm or staff would not allow for the award of variable remuneration.

197. The pay-out of fixed remuneration in instruments, if any, should not impair the ability of the investment firm to apply a fully flexible policy on variable remuneration.

13.2 Ratio between fixed and variable remuneration

198. When setting the fixed remuneration components for staff under Article 30(1), the investment firm should set them at a level that would allow a fully flexible policy on variable remuneration for all staff. To this end the remuneration policy should set an appropriate ratio between the variable and the fixed components of the total remuneration.

199. The ratio set is the ratio between the variable component of remuneration that could be awarded as a maximum for the following performance period and the fixed component of remuneration of the following performance period. The maximum ratios allowable should include levels of pay-outs that would cover 'above target' or exceptional performance and should not only reflect 'on target' or expected performance. The effective ratio between variable remuneration awarded and fixed remuneration should increase with the performance achieved.

200. When setting the ratio, investment firms should take into account their business activities, risks and the impact of the staff or categories of staff on the risk profile of the investment firm or the assets it manages as well as the incentives for staff to act in the best interest of the investment firm and the need to maintain cost flexibility in light of changes of profits and losses over time.

201. When setting the ratio, investment firms should consider that a variable component linked to performance can have a positive effect on 'risk-sharing' and incentivising prudent risk taking

behaviour in line with the investment firms risk appetite, while a variable component that is inappropriately balanced could, under certain circumstances, have negative effects. The higher the possible variable remuneration compared to the fixed remuneration, the stronger the incentive will be to deliver the needed performance, and the bigger the associated risks may become. Investment firms should consider that staff may become accustomed to and expect to receive a considerable variable remuneration. If the fixed component is too low compared to the variable remuneration, an investment firm may find it difficult to reduce or eliminate variable remuneration in a poor financial year.

202. Investment firms may set different ratios for different jurisdictions, different business units, corporate and internal control functions and different categories of staff, e.g. identified staff, unidentified staff responsible for managing assets, sales staff, staff in control functions or staff within administrative functions. In exceptional and duly justified cases, the remuneration policy may provide for a different ratio for individual identified staff members belonging to a certain category of staff compared with other staff members included in the same category of staff.

203. The maximum ratio should be calculated as the sum of all variable components of remuneration that could be awarded as a maximum in a given performance year, including the amount to be taken into account for the retention bonus, divided by the sum of all fixed components of remuneration to be awarded in relation to the same performance year. In any case, all remuneration components should be correctly allocated to either variable or fixed remuneration in line with these guidelines. Investment firms may omit some of the fixed remuneration components where they are immaterial, e.g. where proportionate non-monetary benefits are awarded.

204. The effective ratio should be calculated as the sum of all variable components of remuneration that have been awarded for the last performance year as set out in these guidelines, including amounts awarded for multi-year accrual periods, divided by the sum of fixed components of remuneration awarded for the same performance year. For multi-year accrual periods that do not revolve annually, investment firms may alternatively take into account in each year of the performance period the maximum amount of variable remuneration that can be awarded at the end of the performance period divided by the number of years of the performance period.

205. Investment firms may not take into account the amount of guaranteed variable remuneration awarded that may be awarded as a sign-on bonus to new staff in the calculation of the ratio between the variable and fixed components of the total remuneration for the first performance period when determining if they comply with the ratio set within their remuneration policy.

206. Investment firms should be able to explain the reasoning for the maximum ratios set between the variable and fixed remuneration components through their remuneration policy and how the actual ratios would change compared to the maximum ratio depending on risk and performance indicators.

14. Risk alignment process

207. The risk alignment process includes the performance and risk measurement process (section 14.1); the award process (section 14.2); and the pay-out process (section 15). At each stage of the risk alignment process, the variable remuneration should be adjusted for all current and future risks taken. An investment firm should ensure that incentives to take risks are balanced by incentives to manage risk.

208. An investment firm should align the time horizon of the risk and performance measurement with its business cycle in a multi-year framework. Investment firms should set the accrual period and the pay-out periods for remuneration at an appropriate length, differentiating between remuneration that should be paid upfront and remuneration that should be paid after deferral and retention periods. The accrual and pay-out periods should take into account the business activity and position of the category of identified staff or in exceptional cases of a single identified staff member.

209. Within the risk alignment process, an appropriate combination of quantitative and qualitative criteria in the form of absolute and relative criteria should be used at all stages to ensure that all risks, performance and necessary risk adjustments are reflected. Absolute performance measures should be set by the investment firm on the basis of its own strategy, including its risk profile and risk appetite. Relative performance measures should be set to compare performance with peers, either ‘internal’ (i.e. within the organisation) or ‘external’ (i.e. similar investment firms). Quantitative and qualitative criteria and the applied processes should be transparent and predefined as much as possible. Both quantitative and qualitative criteria may partly rely on judgement.

210. Where judgemental approaches are used, investment firms should ensure a sufficient level of transparency and objectivity when judgements are made by:

   a. setting a clear written policy outlining parameters and key considerations on which the judgement will be based;

   b. providing clear and complete documentation of the final decision regarding the risk and performance measurement or applied risk adjustments;

   c. involving relevant control functions;

   d. considering the personal incentives of the staff making the judgement and any conflicts of interest;

   e. implementing appropriate checks and balances, including, for example, making such adjustments within a panel involving staff from business units, corporate and control functions, etc.;

f. approving the assessment made by a control function or at an appropriate hierarchical level above the function making the assessment, e.g. at the management body in its management or supervisory function or at the remuneration committee.

211. Investment firms should make the risk alignment process transparent to identified staff, including any elements that are based on judgement rather than objective facts or data.

212. Investment firms should provide detailed information to the remuneration committee or to the supervisory function if the final outcome after applying judgemental measures is significantly different from the initial outcome using predefined measures.

14.1 Performance and risk measurement process

213. The variable remuneration of identified staff should be aligned to all risks and the performance of the investment firm, the business unit and the individual. The relative importance of each level of the performance criteria should be determined beforehand in the remuneration policies and adequately balanced to take into account the objectives at each level, the position or responsibilities held by the staff member, the business unit he or she is active in and current and future risks.

14.1.1 Risk assessments

214. The investment firm should define the objectives of the investment firm, business units and staff. These objectives should be derived from its business and risk strategy, corporate values, risk appetite and long-term interests and consider also the cost of capital and the liquidity of the investment firm. The investment firms should assess the investment firm's business units' and identified staff members' achievements during the accrual period against their objectives.

215. Investment firms should take into account all current and future risks, whether on or off-balance-sheet, differentiating amongst risks relevant for investment firm, business units and individuals. Though investment firms usually bear all types of risk at investment firm-wide level, at the level of individual identified staff members or business units only some types of risk may be relevant.

216. Investment firms should also use measures for risk alignment of remuneration where an exact quantification of the risk exposure is difficult, such as reputational and operational risk. In such cases the risk assessment should be based on suitable proxies, including risk indicators, capital requirements or scenario analysis.

217. In order to conservatively take into account all material risks at the investment firm and business unit levels, investment firms should use the same risk measurement methods as used for internal risk measurement purposes, e.g. within the internal capital adequacy assessment process (ICAAP). Investment firms should take into account expected and unexpected losses and stressed conditions.

218. The investment firms should be able to demonstrate to the competent authority how the risk calculations are broken down by business units and different types of risks. The extent and quality of methods and models used within the ICAAP should be reflected by the investment firm in a proportionate way in the remuneration policy.

14.1.2 Risk-sensitive performance criteria

219. Investment firms should set and document both quantitative and qualitative, including financial and non-financial, performance criteria for individuals, business units and the investment firm. The performance criteria should not incentivise excessive risk taking or mis-selling of products.

220. Investment firms should use an appropriate balance between quantitative and qualitative as well as absolute and relative criteria.

221. The criteria used to measure risk and performance should be linked as closely as possible to the decisions made by the identified staff member and the category of staff members subject to the performance measurement and should ensure that the award process has an appropriate impact on staff's behaviour.

222. Performance criteria should include achievable objectives and measures on which the identified staff member has some direct influence. When assessing performance, the effectively realised results and outcomes should be measured.

223. Quantitative criteria should cover a period which is long enough to properly capture the risk taken by identified staff members, business units and the investment firm and should be risk-adjusted and include economic efficiency measures. Investment firms should also use performance criteria for the assets they manage. Examples of quantitative performance measures used in the asset management sector which fulfil the abovementioned provisions are the internal rate of return (IRR), earnings before interest, taxes, depreciation and amortization (EBITDA), Alpha Ratio, absolute and relative returns, Sharpe Ratio and assets raised.

224. Operating efficiency indicators (e.g. profits, revenues, productivity, costs and volume metrics) or some market criteria (e.g. share price and total shareholder return) do not incorporate explicit risk adjustment and are very short-term and therefore not sufficient to capture all risks of the identified staff member's activities. Such performance criteria require additional risk adjustments.

225. Qualitative criteria (such as the achievement of results, compliance with strategy within the risk appetite and compliance track record) should be relevant at an investment firm, business unit or individual level. Examples of qualitative criteria are the achievement of strategic targets, customer satisfaction, adherence to risk management policy, compliance with

internal and external rules, leadership, team work, creativity, motivation and cooperation with other business units, internal control and corporate functions.

14.1.3 Specific criteria for control functions

226. Where control functions' staff receive variable remuneration, it should be appraised and the variable part of remuneration determined separately from the business units they control, including the performance which results from business decisions (e.g. new product approval) where the control function is involved.

227. The criteria used for assessing the performance and risks should predominantly be based on the internal control functions' objectives. Variable remuneration for control functions should predominantly follow from control objectives. Their variable remuneration may also be based to some extent on the performance of the investment firm as a whole. The investment firm should consider setting a significant lower ratio between the variable and the fixed components of remuneration for control functions compared to the business units they control.

228. If the head of the risk management function (Chief Risk Officer or CRO), where established, is also a member of the management body, the principles set out in paragraphs 226 and 227 should also apply to the CRO's remuneration.

229. Where an investment firm does not establish and maintain an audit or risk management function, it should be able to demonstrate upon request that the performance criteria for staff in charge of the related processes do not provide for incentives to perform the control processes inappropriately.

14.2 Award process

230. Investment firms should set a bonus pool. When determining bonus pools or individual awards, investment firms should consider all current risks, expected losses, estimated unexpected losses and stressed conditions associated with the investment firm's activities.

231. Variable remuneration should be awarded after the end of the accrual period. The accrual period should be at least one year. Where longer periods are used, different accrual periods may overlap, for example if a year, a new multi-year period starts each year.

232. After the accrual period, the investment firm should determine the individual identified staff members' variable remuneration by translating the performance criteria and risk adjustments into actual remuneration awards. During this award process, the investment firm should adjust remuneration for potential adverse developments in the future ('ex ante risk adjustment').

14.2.1 Setting of bonus pools for identified staff

233. Investment firms should define one or more bonus pools for the period for which variable remuneration is awarded and calculate the overall investment firm-wide bonus pool for identified staff as a sum of these bonus pools. The bonus pool should be linked to an investment firm's performance. In addition, staff might benefit from appropriate carried interest payments for which no bonus pool is defined.

234. When setting the bonus pools, investment firms should take into account the ratio between the variable and the fixed components of total remuneration applicable to categories of identified staff, performance and risk criteria defined for the overall investment firm, control objectives and the financial situation of the investment firm, including its capital base and liquidity. The performance indicators used to calculate the bonus pool should include long-term performance indicators and take into account the realised financial results. A prudent use of accounting and valuation methods should be in place which ensures a true and fair evaluation of the financial results, capital base and liquidity.

235. The bonus pools should not be set at a certain level to meet remuneration demands.

236. Investment firms should have appropriate processes and controls in place when determining the overall bonus pool.

237. Where investment firms use a top-down approach, they should set the amount of the bonus pool at the level of the investment firm, which is then fully or partially distributed among the business units and control functions after the evaluation of their performance. The individual awards should subsequently be based on the assessment of the individual's performance.

238. Where investment firms set the bonus pool in a bottom-up approach, the process should start at the level of the individual staff member. Depending on the performance criteria by which the staff are assessed, a bonus pool allocation should be made for the staff member; the bonus pool of the business unit and the investment firm equals the sums of potential awards allocated to the respective subordinated levels. The investment firm should ensure that the investment firm's overall performance is appropriately taken into account.

239. When distributing the bonus pool to the level of the business unit or individual staff member, the allocation should be based as appropriate on predefined formulae and judgemental approaches. Investment firms may use scorecards or other appropriate methods to combine different approaches.

240. When choosing the approach, investment firms should take into account the following: formulae are more transparent and, therefore, lead to clear incentives, as the staff member knows all factors determining his or her variable remuneration. However, formulae may not capture all objectives, especially the qualitative ones, which can be better captured by judgemental approaches. The judgemental approach gives more flexibility to management and

can, therefore, weaken the risk-based incentive effect of the performance-based variable remuneration. It should, therefore, be applied with appropriate controls and in a well-documented and transparent process.

241. Factors such as budget constraints, retention of staff and recruiting considerations, subsidisation among business units etc. should not dominate the distribution of the bonus pool as they can weaken the relationship between performance, risk and remuneration.

242. Investment firms should maintain records on how the bonus pool and the staff's remuneration were determined, including how estimates based on different approaches were combined.

14.2.2 The ex ante risk adjustment in the award process

243. Investment firms should determine the bonus pool and variable remuneration to be awarded based on an assessment of performance and risks taken. The adjustment for risks before the award is made ('ex ante risk adjustment') should be based on risk indicators and ensure that the variable remuneration awarded is fully aligned with the risks taken. The criteria used for the ex ante risk adjustment should be sufficiently granular to reflect all relevant risks.

244. Depending on the availability of risk adjustment criteria, investment firms should determine at what level they apply ex ante risk adjustments to the calculation of the bonus pool. This should be at the level of the business unit or at the level of organisational substructures thereof, e.g. the trading desk or the individual staff member.

245. Risk alignment should be achieved by using risk-adjusted performance criteria, including performance criteria that are adjusted for risk based on separate risk indicators. Quantitative and qualitative criteria should be used.

246. The ex ante risk adjustments made by investment firms, where based on quantitative criteria, should largely rely on existing measures within the investment firms, used for other risk management purposes. Where adjustments to such measures are made within risk management processes, investment firms should also make consistent changes in the remuneration framework.

247. When measuring the profitability of the investment firm and its business units, the measurement should be based on the net revenue where all direct and indirect costs related to the activity are included. Investment firms should not exclude costs of corporate functions, e.g. IT costs, group overheads or discontinued businesses.

248. Investment firms should make qualitative ex ante risk adjustments when determining the bonus pool and identified staff's remuneration through, for example, the use of balanced scorecards that explicitly include risk and control considerations such as compliance breaches, risk limit breaches and internal control indicators (e.g. based on internal audit results) or other similar methods.

15. Pay-out process for variable remuneration

249. Without prejudice to the application of waivers under Article 32(4) of Directive (EU) 2019/2034, investment firms should pay the variable remuneration partly upfront and partly deferred and, where required, in instruments and cash in accordance with Article 32 of Directive (EU) 2019/2033. Where a high amount of variable remuneration is paid in instruments, investment firms should consider if the risk alignment with the risk profile of the investment firm or the assets it manages would be improved if a combination of different instruments were awarded. Before paying out the deferred part of cash or the vesting of deferred instruments, a reassessment of the performance and, if necessary, an ex post risk adjustment should be applied to align variable remuneration to additional risks that have been identified or materialised after the award. This applies also where multi-year accrual periods are used.

15.1 Non-deferred and deferred remuneration

250. Without prejudice to the application of waivers under Article 32(4) of Directive (EU) 2019/2034, investment firms should implement a deferral schedule that appropriately aligns the remuneration of staff with the investment firm's activities, business cycle and risk profile and the activities of the identified staff members, so that a sufficient part of the variable remuneration can be adjusted for risk outcomes over time through ex post risk adjustments.

251. A deferral schedule is defined by different components:

   a. the proportion of the variable remuneration that is being deferred (section 15.2);

   b. the length of the deferral period (section 15.2);

   c. the speed at which the deferred remuneration vests, including the time span from the end of the accrual period until the vesting of the first deferred amount (section 15.3).

252. Investment firms should take into account within the deferral schedule the form in which the deferred variable remuneration is awarded and should, where appropriate, differentiate their deferral schedules by varying these components for different categories of identified staff. The combination of these components should lead to an effective deferral schedule, in which clear incentives for long-term-oriented risk taking are provided by transparent risk alignment procedures.

15.2 Deferral period and proportion of deferred remuneration

253. The deferral period starts after the award is made (e.g. at the moment the upfront part of the variable remuneration is paid out). Deferral can be applied to both types of variable remuneration, cash and instruments.

254. When setting the actual deferral period and proportion to be deferred in accordance with the minimum requirements under Article 32(1) (l) of Directive (EU) 2019/2034, investment firms should consider:

a. the responsibilities and authorities by identified staff and the tasks they performed;

b. the business cycle and nature of the investment firm's activities;

c. expected fluctuations in the economic activity and performance and risks of the investment firm and business unit and the impact of identified staff on these fluctuations;

d. the ratio between the variable and fixed components of the total remuneration and the absolute amount of variable remuneration.

255. Investment firms should determine for which categories of identified staff, also considering their roles and responsibilities, deferral periods longer than the required minimum period of at least three to five years should be applied to ensure that the variable remuneration is aligned with the risk profile in the long term. Where longer multi-year accrual periods are used and where the longer accrual period provides more certainty about the risks that have materialised since the beginning of the accrual period, investment firms should consider this fact when setting deferral and retention periods and may, where appropriate, introduce deferral periods that are shorter than the deferral periods which would be appropriate when a one-year accrual period would be used. The minimum requirement of a three-year deferral period applies in any case.

256. Investment firms should set an appropriate portion of remuneration that should be deferred for a category of identified staff or a single identified staff member at or above the minimum proportion of 40%. In case of particularly high amounts of variable remuneration, the proportion of deferral period for such staff members should be of at least 60%.

257. Investment firms should define what level of variable remuneration constitutes a particularly high amount, taking into account the average remuneration paid within the investment firm, when available the EBA remuneration benchmarking report on investment firms and, where available, national and other remuneration benchmarking results and the thresholds set by competent authorities. When implementing the guidelines, competent authorities should set an absolute or relative threshold, considering the above criteria. Remuneration at or above that threshold should always be considered as being of a particular high amount.

258. Where investment firms determine the proportion that is deferred by a cascade of absolute amounts (e.g. part between 0 and 100: 100% upfront; part between 100 and 200: 50% upfront and the rest is deferred; and part above 200: 25% upfront and the rest is deferred), investment firms should be able to demonstrate to the competent authority that on an average weighted basis for each identified staff member the investment firm respects the 40% to 60% minimum

deferral threshold and that the deferred portion is appropriate and correctly aligned with the nature of the business, its risks and the activities of the member of identified staff in question.

259. Where the general principles of national contract and labour law prevent the substantial reduction of variable remuneration where subdued or negative financial performance of the investment firm occurs, investment firms should apply a deferral scheme and use instruments for the award of variable remuneration that ensure that ex post risk adjustments are as far as possible applied. This may include any of the following:

a. setting longer deferral periods;

b. avoiding the use of pro rata vesting in situations where malus can be applied, but the application of clawback would be subject to legal impediments;

c. awarding a higher portion of variable remuneration in instruments that are aligned to the performance of the investment firm and subject to sufficiently long deferral and retention periods.

15.3 Vesting of deferred remuneration

260. The first deferred portion should not vest sooner than 12 months after the start of the deferral period. The deferral period ends when the awarded variable remuneration has vested or where the amount was reduced to zero as malus was applied.

261. Deferred remuneration should either vest fully at the end of the deferral period or be spread out over several payments in the course of the deferral period in accordance with Article 32(3) of Directive (EU) 2019/2034.

262. Pro rata vesting means, for example, a deferral period of four years that at the end of years n+1, n+2, n+3 and n+4, one quarter of the deferred remuneration vests, with n being the moment at which the upfront part of awarded variable remuneration is paid.

263. Vesting should not take place more frequently than on a yearly basis to ensure a proper assessment of risks before the application of ex post adjustments.

15.4 Award of variable remuneration in instruments

264. The instruments used for the award of variable remuneration should contribute to the alignment of variable remuneration with the performance and risks of the investment firm.

265. Investment firms should prioritise the use of instruments, as set out in Article 32 (j) of Directive (EU) 2019/2034, issued by the investment firm itself. Investment firms may also use the instruments listed in points (i), (ii) and (iii) of Article 32(j) of Directive (EU) 2019/2034 issued within the scope of consolidation. The variable remuneration may consist of a balance of different types of instruments.

266. Where an investment firm does not issue any eligible instruments, but does not benefit from a waiver under Article 32(4) of Directive (EU) 2019/2034, it should apply for the use of an alternative arrangement, demonstrating that it does not issue such instruments.

267. Competent authorities, when deciding on applications to use alternative arrangements, should take into account:

a. that investment firms which are stock corporations (both listed and non-listed) have issued shares and therefore in general shares and in any case share-linked instruments are available for the pay-out of variable remuneration;

b. if it would be possible and proportionate for the investment firm to make use of share-linked instruments or equivalent non-cash instruments, subject to the legal structure of the investment firm;

c. if 'other instruments' under Article 32(j)(iii) of Directive (EU) 2019/2034 have been issued, which depends on whether an investment firm or an investment firm in the scope of consolidation has already issued such instruments and sufficient amounts of such instruments are available. Where investment firms are primarily wholesale funded, or rely to a large extent on additional Tier 1, Tier 2 or bail-in-able debt to meet their capital requirements, such instruments should be available for the purposes of variable remuneration, provided that these 'other instruments' comply with Commission Delegated Regulation mandated under the IFD;

d. If there are specific requirements under national labour law that prevent the use of an issued eligible instrument for the pay-out of variable remuneration.

268. Share-linked or other equivalent non-cash instruments (e.g. stock appreciation rights, types of synthetic shares) are those instruments or contractual obligations, including instruments based on cash, whose value is based on the market price or, where a market price is not available, the fair value of the stock or equivalent ownership right and track the market price or fair value. All such instruments should have the same effect in terms of loss absorbency as shares or equivalent ownership interests.

269. Investment firms should ensure that they have the awarded instruments available when the variable remuneration awarded in instruments vest. Investment firms may decide not to hold the instruments during the deferral period, but should in that case take into account the relevant market risks.

270. Instruments should be priced at the market price or their fair value on the date of the award of these instruments. This price is the basis for the determination of the initial number of instruments and for later ex post adjustments to the number of instruments or their value. Such valuations should also be done before the vesting to ensure that ex post risk adjustments are applied correctly and before the retention period ends. Investment firms that are not listed

may establish the value of the ownership interests and ownership interest-linked instruments based on the last annual financial results.

271. Investment firms may award a fixed number or nominal amount of deferred instruments using different techniques, including trustee depot facilities and contracts, provided that in every case, the number or nominal amount of the instruments awarded is provided to identified staff at vesting, unless the number or nominal amount is reduced by the application of malus. Investment firms should make sure that the awarded instruments are available for the pay out to staff at the latest when they vest.

272. Investment firms should not pay any interest or dividend on instruments which have been awarded as variable remuneration under deferral arrangements to identified staff; this means also that interest and dividends payable during the deferral period should not be paid to staff after the deferral period ends. Such payments should be treated as received and owned by the investment firm. The same should apply for non-cash instruments which reflect the instruments of the portfolios managed.

15.5 Minimum portion of instruments and their distribution over time

273. Where applicable, the requirement to pay, in accordance with Article 32(1)(j) of Directive (EU) 2019/2034, at a minimum 50% of any variable remuneration in instruments. Investment firms should apply this requirement either equally to the non-deferred and the deferred part or choose to award a higher portion of the deferred part of remuneration in instruments, as long as in total the minimum requirement of 50% is met.

274. Investment firms should prioritise the use of instruments rather than award variable remuneration in cash. Investment firms should set the percentage which is awarded in instruments at or above 50%. Where investment firms award a higher portion than 50% of the variable remuneration in instruments, they should prioritise a higher share of instruments within the deferred portion of the variable remuneration component.

275. The ratio of variable remuneration that is paid out in instruments should be calculated as the quotient between the amount of variable remuneration awarded in instruments and the sum of the variable remuneration awarded in cash, instruments and in any other form. All amounts should be valued at the point of award unless stated otherwise in these guidelines.

15.6 Retention policy

276. The retention period applied to variable remuneration paid in instruments should be set at an appropriate length in order to align incentives with the longer-term interests of the investment firm.

277. The investment firm should be able to explain how the retention policy relates to other risk alignment measures and how they differentiate between instruments paid upfront and deferred instruments.

278. When setting the retention period, investment firms should consider the overall length of the deferral and the planned retention period and the impact of the category of identified staff on the investment firms' risk profile and the length of the business cycle relevant for the category of staff.

279. A longer retention period as applied in general to all identified staff should be considered in cases where the risks underlying the performance can materialise beyond the end of the deferral and standard retention period, at least for the staff with the highest impact on the investment firms' risk profile.

280. For awarded instruments, a retention period of at least one year should be set. Longer periods should be set in particular where ex post risk adjustments mainly rely on changes of the value of instruments which have been awarded. Where the deferral period is at least five years, a retention period for the deferred part of at least six months may be imposed for identified staff other than members of the management body and senior management for whom a minimum retention period of one year should be applied.

15.7 Risk adjustment

15.7.1 Malus and clawback

281. Malus or clawback arrangements are explicit ex post risk adjustment mechanisms where the investment firm itself adjusts remuneration of the identified staff member based on such mechanisms (e.g. by lowering awarded cash remuneration or by reducing the number or value of instruments awarded).

282. Without prejudice to the general principles of national contract or labour law, investment firms must be able to apply malus or clawback arrangements up to 100% of the total variable remuneration in accordance with Article 32(1)(m) of Directive (EU) 2019/2034 regardless of the method used for the payment, including deferral or retention arrangements.

283. Ex post risk adjustments should always be performance or risk-related. They should respond to the actual risk outcomes or changes to persisting risks of the investment firms, business line or staff's activities. They should not be based on the amount of dividends paid or the evolution of the share price.

284. Investment firms should analyse whether their initial ex ante risk adjustments were sufficient, e.g. whether risks have been omitted or underestimated or new risks were identified or unexpected losses occurred. The extent to which an ex post risk adjustment is needed depends on the accuracy of the ex ante risk adjustment and should be established by the investment firm based on back-testing.

285. When setting criteria for the application of malus and clawback in accordance with Article 32(1)(m) of Directive (EU) 2019/2034, investment firms should also set a period during which malus or clawback will be applied to identified staff. This period should at least cover deferral and retention periods. Investment firms may differentiate between criteria for the application of malus and clawback. Clawback should in particular be applied in the case of fraud or other conduct with intent or severe negligence which led to significant losses.

286. Investment firms should use at least the initially used performance and risk criteria to ensure a link between the initial performance measurement and its back-testing. Investment firms should, in addition to the criteria set out in Article 32(1)(m)(i) and (ii) of Directive (EU) 2019/2034, use specific criteria including:

a. evidence of misconduct or serious error by the staff member (e.g. breach of code of conduct and other internal rules, especially concerning risks);

b. whether the investment firm and/or the business unit subsequently suffers a significant downturn in its financial performance (e.g. specific business indicators);

c. whether the investment firm and/or the business unit in which the identified staff member works suffers a significant failure of risk management;

d. significant increases in the investment firm's or business unit's economic or regulatory capital base;

e. any regulatory sanctions, e.g. punitive, administrative, disciplinary or otherwise, where the conduct of the identified staff member contributed to the sanction.

287. Where malus can only be applied at the moment of vesting of the deferred payment, investment firms may choose, where possible, to apply clawback after paying out or vesting of the variable remuneration. The application of malus may not be possible where the derogation under Article 32(4) of Directive (EU) 2019/2034 applies as the requirement to defer variable remuneration is not applied; investment firms should ensure that clawback can be applied.

288. Malus and clawback arrangements should lead to a reduction of the variable remuneration where appropriate. Under no circumstances should an explicit ex post risk adjustment lead to an increase of the initially awarded variable remuneration or, where malus or clawback was already applied in the past, to an increase of the reduced variable remuneration.

15.7.2 Implicit adjustments

289. Investment firms should use instruments for variable remuneration where the price reacts to changes of the investment firm's performance or risk. The evolution of the stock price or the price of other instruments should not be considered as a substitute for explicit ex post risk adjustments.

290. Where instruments were awarded and staff, after deferral and retention periods, sell these instruments or the instrument is paid out in cash at its final maturity, staff should be able to receive the amount due. The amount can be higher than the initially awarded amount where the market price or the instrument's fair value has increased.

Title V – Investment firms that benefit from government intervention

16. State support and remuneration

291. In line with section 6 of these present guidelines, where investment firms benefit from exceptional government intervention, competent authorities and investment firms should establish regular contacts with regard to the setting of the bonus pool of possible variable remuneration and the award of variable remuneration to ensure compliance with Article 31 of Directive (EU) 2019/2034 and any additional restrictions imposed by competent authorities. Any payment of variable remuneration should not endanger compliance with the established recovery and exit plan from exceptional government intervention.

292. For investment firms that fall under the scope of Directive 2014/59/EU, the Communication from the Commission on the application, from 1 August 2013, of State aid rules to support measures in favour of banks in the context of the financial crisis (2013/C 216/01) should be applied within the remuneration policies. Any condition with regard to remuneration imposed on investment firms when state aid has been approved by the Commission and granted and within any related acts should be reflected appropriately in the investment firms' remuneration policy.

293. The variable remuneration of an investment firm's staff should not prevent an orderly and timely payback of the exceptional government intervention or the achievement of objectives set in the restructuring plan.

294. The investment firm should ensure that a bonus pool or the vesting and paying out of variable remuneration do not pose damage the timely building up of its capital base and a decrease in its dependence on exceptional government intervention.

295. Competent authorities should monitor that the investment firm complies with the conditions of Article 31 of Directive (EU) 2019/2034 and may set a maximum percentage of the net revenue that can be used for the pay-out of variable remuneration.

Title VI - Competent authorities

17. Remuneration policies

296. Competent authorities should apply a risk-based approach when supervising the remuneration policies and practices of investment firms and review them in line with the EBA guidelines on the supervisory review process.

297. Competent authorities should ensure within their supervisory review, taking into account these guidelines, that investment firms comply with the requirements on remuneration policies set out in Directive (EU) 2019/2034 and the provisions of the RTS on identified staff, including that they have appropriate gender neutral remuneration policies for all staff and for identified staff.

298. Competent authorities should ensure that investment firms align their remuneration policy and practices to the business strategy and the long-term interest of the investment firm taking into account its business and risk strategy, corporate culture and values, and risk profile.

299. Competent authorities should ensure that investment firms' remuneration policies, practices and processes are appropriate, including the award of guaranteed variable remuneration, severance payments and discretionary pension benefits.

300. Competent authorities should ensure that investment firms have set an appropriate maximum ratio between the variable and the fixed part of total remuneration.

301. Competent authorities should review the gender pay gap within investment firms and follow up on any indication that remuneration policies are not gender neutral.

302. Competent authorities should be satisfied with the overall outcome of the identification process and should assess if all staff members whose activities have or may have a material impact on the investment firm's risk-profile or of the assets that it manages have been identified and that any exclusions of staff from the category of identified staff, where staff were only identified by the quantitative criteria in the RTS are well-reasoned and that the respective processes set out in these guidelines and the RTS have been complied with.

303. Without prejudice to other supervisory and disciplinary measures and sanctions, competent authorities should require investment firms to take adequate actions in order to remedy any identified deficiencies. Where investment firms do not comply with such request, appropriate supervisory measures should be taken.

20. Disclosures

304. Competent authorities should review the public disclosures on remuneration made by investment firms in accordance with Article 51 of Regulation (EU) 2019/2033, and should establish for which investment firms a regular review of disclosures should be performed.

305. In addition to the benchmarking of remuneration practices required under Article 34(1) of Directive (EU) 2019/2034 and the exercise on data collection regarding high earners under Article 34(4) of that Directive, competent authorities should require periodic (or ad hoc) supervisory reporting on remuneration disclosures as appropriate in order to monitor the development of remuneration practices within investment firms and in particular within the largest investment firms in that Member State.

21. Colleges of supervisors

306. Colleges of supervisors established pursuant to Article 48 of Directive (EU) 2019/2034 should discuss remuneration issues in line with the supervisory review process, taking into account the additional areas of supervisory review required under these guidelines.

5. Accompanying documents

5.1 Cost-benefit analysis/impact assessment

1. Article 16(2) of Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority) (EBA Regulation) provides that the EBA should carry out an analysis of ‘the potential related costs and benefits’ of any guidelines it develops. This analysis should provide an overview of the findings regarding the problem to be dealt with, the solutions proposed and the potential impact of these options.

A. Problem identification and policy objectives

2. Directive (EU) 2019/2034 is replacing for investment firms the requirements on remuneration policies that have previously been encoded in Directive 2013/36/EU (CRD). The EBA has been mandated to develop the present guidelines.

B. Baseline scenario

3. The current EU legislative framework for investment firms’ remuneration policies consists mainly of Directive 2013/36/EU and the EBA guidelines on sound remuneration policies, guidelines on the collection of data on high earners and on the remuneration benchmarking exercise. The framework set under IFD is largely equivalent to the framework under CRD.

4. The impact assessment covers guidelines developed to ensure the harmonised application of remuneration requirements introduced by Directive (EU) 2019/2034 where they differ from the previously applicable framework. The assessment is limited to areas where the guidelines have changed compared to the framework established as applicable on 28 December 2020 (CRD V). Areas that have not changed in substance and the changes introduced within the Directive (EU) 2019/2034 (IFD) and Regulation (EU) 2019/2033 have not been assessed.

C. Options considered

5. With regard to aspects that have been changed within CRD V, the EBA has already published a consultation paper on revised remuneration policies, including an impact assessment on gender neutral remuneration policies, retention bonuses and severance payments. The present consultation paper includes the same changes and therefore no additional impact assessment is made for those aspects.

Implementation date.

6. Specific requirements on remuneration policies are being introduced for investment firms by implementation of Directive (EU) 2019/2034 into national law on 26 June 2021.

7. Considering that the IFD remuneration framework as such is equivalent to the requirements under CRD, a short implementation period is sufficient. Some of the requirements under the IFD require changes to remuneration policies and investment firms' governance arrangements. This concerns, for example, the establishment of a remuneration committee and the setting of a ratio for variable remuneration to fixed remuneration for all staff. An application date of 31 April 2022 appears appropriate to allow investment firms that have not been subject to the CRD provisions to establish internal remuneration policies in line with the provisions set out in the guidelines

8. Transitional provisions have been added to ease the challenges of investment firms to document any changes made and to allow for an effective implementation of the guidelines, taking into account to have in some situations an adoption of policies by shareholders.

Remuneration policies for all staff

9. The IFD requires investment firms to set an appropriate ratio between the variable and the fixed remuneration for all staff. Guidance has been provided on how investment firms should set such a ratio within their remuneration policy.

   Option A: The guidelines should set out the considerations that investment firms should take into account when setting the ratio, how it is calculated and give guidance on the expectations regarding the implementation in throughout the investment firm. Such guidance would ensure an appropriate framework so that competent authorities can supervise the setting of the ratio. A more procedural approach would give the investment firm the responsibility to set the appropriate ratio, but require investment firms to be able to demonstrate the appropriateness of their policy.

   Option B: In addition to Option A, a range of ratios should be set that in general are considered as appropriate.

   Option A would lead to some additional costs for the competent authority compared to maintaining Option B; the appropriateness of the ratio also has to be supervised in any case, but on a risk-based approach. However, Option B might be perceived as imposing restrictions and would run the risk of investment firms not being able to align their remuneration policy with their risk profile and national remuneration practices. As those investment firms do not pose a systemic risk to the financial system, it is not necessary to strictly limit the ratio for that reason. While it is a competent authority's obligation to supervise the prudential risks the policy could cause in terms of reducing the soundness of the capital, the approach taken also

relies on the control by owners and markets so that the distribution of profits between owners, investors and staff is appropriate.

Option A has been retained.

Monitoring the gender pay gap

10. IFD requires investment firms to submit information on the gender pay gap to competent authorities. In addition IFR requires specific disclosure requirements. The guidelines should provide for some provisions that allow competent authorities to benchmark trends regarding the gender pay gap.

    Option A: Limit monitoring of the pay gap to identified staff

    While this approach would be consistent with disclosure requirements, it would not be effective as the issue of the gender pay gap may concern all staff. Given different levels of pay at different levels of seniority, an overall benchmark based on all identified staff or all staff would lead to figures that are difficult to interpret, as the gap may depend on random effects resulting from having one gender better represented at the level of the highest paid staff. Moreover, members of the management body in the supervisory function receive in most cases no remuneration, but a fee for their services and participation.

    Option B: Perform the monitoring of the pay gap for the different functions within the management body, identified staff and other staff.

    The approach would overcome the above-described differences. The allocation of staff to those groups is anyway required, in the same way the collection of remuneration data has to be done separately under IFD/IFR requirements. Hence there is no material additional burden for this more granular monitoring and reporting. Disclosure would still follow a less granular approach.

    Option C: Monitoring on a country-by-country basis

    Most investment firms will be active mainly in one Member State. However, the establishment of branches and provision of services is also possible in other Member States. Moreover, the need to monitor the gender pay gap and to inform the competent authority applies also on consolidated level. Given material differences in remuneration levels and pools of available human resources per gender may differ between Member States, therefore monitoring country by county would be more effective. To reduce the burden and to avoid an analysis based on small groups of staff, this approach should only be taken in firms that have at least 50 staff. This number is in line with the Commission Recommendation C(2014) 1405 final.

    Option B and C have been retained.

Pay-out in instruments

11. Investment firms have to pay a part of the variable remuneration in instruments. Guidance on the instruments and the ratio is provided.

12. Option A: In line with the approach taken under the CRD allowing the use of shares, share linked, AT 1 and AT 2 and other instruments issued in a group context if there is a link to the risk profile.

13. Option B: Allowing also the use of instruments that reflect the instruments of the portfolios managed in a group context.

14. Option C: Requiring that the 50% of variable remuneration that has to be paid in instruments should be either equally applied for the deferred and non-deferred part or that a higher ratio of deferred remuneration should be paid in instruments.

    Regarding Option A, any additional restrictions would lead to additional costs and therefore Option A was retained even if instruments issued, e.g. by a parent credit institution, are not leading to a strong alignment of the risk to clients with the remuneration paid in instruments. However, it could be disproportionate to use a stricter approach for investment firms as compared to credit institutions. Where investment firms manage portfolios, such instruments that are linked to the assets they manage should refer to the assets managed by the investment firm to ensure an alignment of remuneration with the risks to assets. Even if there is a small additional cost for creating instruments on an individual level and considering that the IFD does not require a balance of different instruments to be used, Option B has not been retained. Option C has been retained as the alignment of remuneration to risk increases if the pay-out in instruments concerns deferred remuneration. There are no additional costs as compared to an approach where the minimum ratio is applied equally to the deferred or non-deferred part.

    Options A and C have been retained.

E. Cost-benefit analysis

Given the limited changes compared to the baseline scenario and the easing of some requirements within IFD and the guidelines, it is assumed that the changes to the guidelines as such create low implementation costs mainly for updates to internal policies and additional required documentations.

5.2 Feedback on the public consultation and the opinion of the Banking Stakeholder Group

Summary of key issues and the EBA's response

The guidelines have been consulted on for a three-month period until 17 March 2021. The EBA received overall 15 responses, of which 14 have been published. One was submitted on a confidential basis. In addition, the EBA's Banking Stakeholder Group (BSG) submitted its advice.

Most respondents noted that the date of application is too ambitious and investment firms need some time for internal implementation of the new guidelines.

Some respondents found that the framework under the guidelines is very similar to the framework under the CRD. Respondents proposed to introduce more references to the application of proportionality.

A few respondents highlighted the importance of avoiding 'conflicts of laws' among the guidelines and national social and labour legislations or conflicts with regard to collective bargaining, in particular concerning gender neutral remuneration policies. Furthermore, it was found that the provisions on anti-discrimination and equal opportunities would go beyond the requirement to have gender neutral remuneration policies.

Some respondents wondered why the thresholds for waivers and the calculation of the ratio between variable and fixed remuneration followed a different approach.

Views of the BSG[22]

The BSG submitted its comments to the draft GL during the period of public consultation. In general, the BSG is supportive with regard to many parts of the guidelines, including the provisions on waivers, performance criteria and pay-out in instruments and suggested further clarifications in some areas.

Among other points, the BSG suggested to further clarify the application of the proportionality principle and to detail the level of sophistication expected from different investment firms. The BSG notes that the requirements addressed to competent authorities appear to be limited, since – compared to the CRD guidelines – some indications have been removed on how supervisors could assess the appropriateness of firms' remuneration policies.

The BSG also outlines that, with regard to gender pay neutrality, some additions to the text are needed to embed the Level 1 text and ensure that gender neutral remuneration policies are effectively and consistently applied in practice. The BSG also expressed the view that the EBA should take due account of the rights of employee representatives and trade unions under national law, as well as the payments agreed in collective bargaining.

[22] The response of the BSG is available under: https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Consultations/2021/Consultation%20on%20Guidelines%20on%20remuneration%20policies%20for%20investment%20firms/964578/BSG%20on%20GL%20on%20remuneration%20policies%20for%20investment%20firms.pdf

EBA's response

The EBA has taken into account the comments received and the opinion of the Banking Stakeholder Group and revised the guidelines. Where appropriate, the EBA has also aligned the guidelines with changes made to the guidelines under CRD.

The guidelines provide a set of criteria that should be taken into account when applying the guidelines in a proportionate manner. Providing for specific thresholds or criteria, which would demand the implementation of specific provisions, as suggested, would reduce the flexibility of investment firms and competent authorities. Given the multitude of different but overlapping business models, such a system of specifications would potentially lead to an unlevel playing field in certain areas.

The guidelines aim to further specify requirements under the IFD and to achieve harmonisation at the EU level. Given the need of Member States to implement the CRD provisions and to abide by the principles set out within the European Charter of Fundamental Rights, it would be surprising if social or labour law, including collective bargaining, would lead to results that are not gender neutral. Therefore, it is presumed that the guidelines do not lead to any conflicts regarding those matters. However, the obligation to ensure a gender neutral remuneration policy applies to the investment firms and not the social partners that negotiate employment conditions.

All aspects of the remuneration policy must be gender neutral. Some aspects concerning equal opportunities and anti-discrimination have been further specified in the EBA guidelines on internal governance under IFD. However, some aspects have also been retained in these guidelines as they are linked to the remuneration of staff.

The different calculation of amounts regarding the application of waivers under Article 32 of the IFD and the application of the maximum ratio set by the investment firm in the context of severance payments have been retained, but have been further specified. The calculation differs as the context and the underlying provisions of the IFD differ. The thresholds for the application of waivers are set out in the IFD and cannot be increased by guidelines. The waivers introduced and thresholds set by the co-legislators have the purpose of reducing the burden for the pay-out of a part of the variable remuneration in instruments and under deferral arrangements, in situations where only a low amount is paid. Where in fact a higher amount is paid out, the prudential benefits of applying those requirements exceed the burden for their application.

The different calculation of amounts in the context of severance payments is a technical necessity and ensures that the limitation of the ratio between variable and fixed remuneration set within the investment firm's policy can be applied in a meaningful way. The calculation of a ratio with regard to severance payments differs, as the payment is made for the early termination of a contract and not for a defined performance period, so that a ratio between the variable and fixed remuneration for such elements can hardly be calculated.

More detailed feedback on the comments is included in the following feedback table.

Summary of responses to the consultation and the EBA's analysis

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
General comments			
Date of application	Some respondents observe that some investment firms that are subject to the guidelines have not been subject to CRD in the past and must comply for the first time with detailed remuneration requirements, in particular the identification of risk takers and the pay-out rules, which may require considerable implementation effort. Some respondents would find it helpful if the guidelines made it clear that the transitional timelines apply to the remuneration requirements of Directive (EU) 2019/2034 itself, as well as to these EBA guidelines. Another respondent requests that the EBA provide more clarity regarding the application of the transitional provisions to the remuneration structure requirements, since the draft guidelines do not specify the date on which the remuneration structure requirements (e.g. the pay-out process rules and related provisions) apply, so that it would be unclear whether firms are required to apply the remuneration structure requirements by 26 June 2021 (e.g. the current performance year) or whether such requirements are subject to the transitional provisions and do not apply until 1 January 2022. A respondent, while appreciating the transitional period provided, points out that any changes to individual contracts may need a longer period for implementation due to the rights of staff under labour laws, and believes that this should be adequately reflected under paragraph 11.	The date of implementation has been moved back to 31 April 2022. The set date of application should provide for sufficient time to implement the guidelines and aligns their application with the calendar year. The IFD does not contain transitional arrangements for the application of remuneration requirements that are further specified within these guidelines. The application of IFD provisions cannot be altered by the means of EBA guidelines.	GL amended
Impact assessment	One respondent raised concerns regarding the very limited scope of the impact assessment. The EBA is reminded that many firms now subject	As explained in the impact assessment section, the EBA's impact assessments are limited to the impact caused by the	No change

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
	to IFD would have been exempt from remuneration rules under CRD on the principle of proportionality and non-significance.	guidelines and do not assess the impact created by the implementation of IFD. Different waivers have been introduced within the CRD and IFD for certain remuneration provisions. Such waivers did not exist beforehand in the respective level-1 texts at EU level.	
Policies for all staff	Some respondents ask for clarification on the application of remuneration policies to all staff and to identified staff. In particular, a respondent disagrees with the proposed scope that the remuneration policies and practices shall apply to all staff. According to the respondent, remuneration policies for all staff should be limited to (1) the application of the principle of equal pay for male and female workers for equal work or work of equal value and (2) clear principles on how to align remuneration with the risk profile of investment firms, while all other requirements on the remuneration policies should be limited to identified staff members and to the content defined in Article 30 IFD.	Article 26 IFD requires investment firms to have remuneration policies that are gender neutral. Those policies should apply to all staff. Investment firms should also have policies for their tied agents, as they are in the scope of prudential consolidation. It should be ensured that the use of tied agents should not led to a circumvention of the remuneration requirements. The remuneration policies for identified staff must comply with the requirements under Articles 30 and 32 of the IFD. Investment firms should consider if it would be appropriate to apply such elements or parts of them also to all staff as part of the firm's policy.	No change
Principle of proportionality	Some respondents, while appreciating the acknowledgement that the guidelines should be applied with due regard to the principle of proportionality, believe that the principle of proportionality is not reflected in several areas set out in the guidelines and that it could be further strengthened in particular in how it applies to the structure of remuneration (Section III). In addition, the guidelines are based on hard quantitative thresholds, which are not deemed appropriate for asset managers holding a MiFID license. A respondent highlights that the amount of assets under management could not be a stand-alone criterion for a risk measurement approach, since also the nature, scope and complexity of the activities should be	The guidelines specify the provisions within the IFD. The principle of proportionality ensure that the respective provisions are applied in an appropriate manner. The guidelines provide for the needed flexibility. Given the multitude of different but overlapping business models, a system of specifications e.g. per authorised activity would potentially lead to an unlevel playing field in certain areas. Additional waivers on top of the ones included in the IFD cannot be granted by means of guidelines.	No change

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
	relevant (such as the underlying risk profiles of the business activities that are carried out). One respondent suggested including indications of investment services and activities for which a greater degree of sophistication is expected, but consider that points (8) [operation of an MTF] and (9) [operation of an OTF] of Section A of Annex 1 to Directive 2014/65/EC (MiFID 2) also require a high degree of sophistication, particularly because in the case of OTFs, there may be few alternative regulated venues available on which to trade a particular financial instrument. Some respondents suggested that the proportionality principle may allow for different governance structures (provided that the high-level requirements of the IFD/IFR are met) and for a greater amount of flexibility with respect to each remuneration parameter (including structure and deferral period, retention structures, procedures for risk adjustment) as compared to the framework under CRD.	All criteria provided for in the guidelines need to be considered in parallel, however, waivers are based on fixed thresholds. The requirements on the variable remuneration under IFD are very similar to the requirements under CRD. Most investment firms have been subject to those requirements. The guidelines cannot alter the application of minimum requirements included in the IFD, e.g. regarding deferral ratios and periods and should ensure that the objectives, namely an alignment between risk profile and variable remuneration, are indeed achieved.	
Principle of proportionality	Some respondents commented that guidelines under CRD for significant institutions should not be automatically carried forward under IFD, since their application to investment firms with a balance sheet above EUR 100 million does not appear adequate and proportionate.	Specific provisions for significant investment firms have been removed from the guidelines. The proportionality criteria have been reviewed.	GL amended
Impact of variable remuneration on capital base	A respondent suggests reflecting in Section 6 on capital base that an extensive use of variable remuneration to key members of staff can lower a firm's exposure to operational costs, which mainly is made up of salaries, in case of falling revenues from asset management services.	The EBA is well aware of the impact of fixed remuneration on the fixed overheads of an investment firm. However, the underlying provisions are part of the IFD/IFR and cannot be changed via guidelines. At the same time, some fixed remuneration is required under IFD to ensure that the firm can comply for its identified staff with the requirements under Articles 30 and 32 of the IFD.	No change

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
EBA guidelines and national legislations	A respondent points out the importance for these guidelines of not creating a conflict of law with national social and labour legislations, which would lead to a situation where actors scoped in are not able to comply both with the guidelines and with national legislations that the IFD does not amend.	Member States are required to implement the IFD, in some cases this might create the need to also change other laws that are not directly targeted by the IFD. However, it would be surprising if, for example, provisions on gender neutral remuneration or anti-discrimination would conflict with the principles encoded in national social or labour law.	No change
Background and rationale Para. 7 Report on the application of gender neutral remuneration policies	A respondent asks for greater clarity about the report that the EBA is mandated to issue on the application of gender pay neutral policies and how this may impact the current requirement of the IFD and other Directives.	The report will review the application and provide its findings to the European Commission and national competent authorities. Depending on the findings further legislative measures might follow. This is, however, not for the EBA to decide on.	No change
Para. 168 Custodial accounts	A respondent asks for the final sentence of the paragraph to be removed from the guidelines, since the proposed requirement for staff to notify the firm of any custodial accounts outside the investment firm is disproportionate, goes beyond the personal account dealing requirements under MiFID and would require firms to impose an intrusive requirement on staff. It is also pointed out that the two most conspicuous ways in which staff might seek to hedge against the IFD remuneration requirements are insurance policies or derivative transactions, neither of which are typically held in custodial accounts.	While it is true that not each and every hedging attempt can be prevented, this provision has been retained, as it is an effective measure to enable investment firms to monitor if staff comply with the requirements.	No change
Para. 227 Bonus pool	A respondent, whilst recognising that investment firms must not undermine their capital and liquidity requirements, deems it inappropriate and disproportionate to require some firms (such as MiFID 'adviser-arranger' entities within alternative asset management groups, which have predictable revenue streams, for example advisory	Investment firms should set bonus pools for their identified staff, who should receive a performance related remuneration. This part of the variable remuneration allows the staff to benefit from the overall profits.	GL amended

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
	fees charged on a 'cost-plus' basis) to set bonus pools and comply with associated obligations. It is remarked that allowing greater flexibility would make sense purposively for such firms, where the most substantial part of remuneration awards typically takes the form of carried interest awards rather than bonuses.	Carried interests are defined as a share of generated profit of a portfolio and allows staff to benefit from the performance of the portfolio. The guidelines have been clarified.	
Para. 293 Requirements for competent authorities	A respondent recognises that some flexibility is needed to ensure that supervision is risk-based, but is concerned that this could lead to inconsistent and potentially ineffective approaches being taken and undermine the impact of the guidelines. The respondent suggested clarifications to the section on risk-based supervision.	The supervisory processes for investment firms will be subject to a separate set of guidelines. The present guidelines consulted on the areas that should be reviewed by supervisors.	No change
Responses to questions in Consultation Paper EBA/CP/2020/26			
Question 1. Are the subject matter, scope and definitions appropriate and sufficiently clear?			
Disclosure requirements	Some respondents note that the guidelines do not include any guidance on the implementation timeline for disclosure requirements under Article 51 of Regulation (EU) 2019/2033. They suggest that such requirements should only apply in respect of remuneration awarded under policies that are subject to the remuneration policy and governance requirements within the IFD/IFR package. Hence, the remuneration disclosure requirements should only apply to remuneration awarded in respect of performance years starting after 31 December 2021.	Disclosure requirements are included in the IFD/IFR package. The IFR is directly applicable EU law. IFD requires Member States to implement the requirements into national law by 26 June 2021. The date of application of the IFR requirements is set at the level 1 text and cannot be altered by guidelines.	No change
Para. 8 Scope of application	Some respondents ask for the scope of the EBA guidelines to be clearly limited to the Level 1 scope of investment firms in the meaning of Article 2 IFD (authorised and supervised under MiFID II) which do not meet the conditions of Article 12 IFR.	The consulted guidelines follow the suggested approach. The scope of the guidelines is clearly limited to investment firms that are subject to the IFD.	No change

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
	A respondent notes that the guidelines are addressed to '*financial institutions as referred to in Article 4 (1) of Regulation (EU) No 1093/2010 that are investment firms as defined in Article 4(1)(1) of Directive 2014/65/EU and do not meet all of the conditions to qualify as small and non-interconnected investment firms under Article 12(1) of Regulation (EU) 2019/2033*' and claims that, being the definition of investment firm taken from MIFID II, all credit institutions would also be within the scope of these GLs, as they are financial institutions that are investment firms under MiFID II. Since this cannot have been the intent of the EBA (which is also mandated to adopt separate GLs specifically for credit institutions), the respondent asks for the EBA to change the addressees of the GL in a way that credit institutions are clearly excluded from their scope of application.		
Para. 9 Definitions	A respondent, noting that the definition of 'remuneration' includes carried interests within the meaning of Article 4(1)(d) AIFMD, states that carried interests are not a 'remuneration' but an incentive model comparable to a very specific type of performance fee, and that the typical carried interest model always satisfies the inherent policy intent of remuneration regulation (i.e. carried interest is only paid out once the external investors have received back all of their drawn-down capital, plus an agreed preferred return). Finally, it is requested to clarify that any returns from co-investments in funds, where they represent a pro-rata return on investments made by firm's staff members, should not be subject to the IFD guidelines.	Payments received as carried interest are to be treated as variable remuneration. This is in line with the framework provided under the AIFMD.	No change
Para. 9 Definitions	With specific regard to the definition of 'retention bonus', the respondents recommend amending it in order to make it clear that deferred compensation grants (i.e. compensation granted as the deferred portion of an annual bonus) are not intended to be included within the scope of the definition.	Deferral is a mechanism that can or has to be applied to variable remuneration. There are only two types of remuneration. Fixed remuneration that meets all the specifications provided in the guidelines and variable	No change

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
		remuneration, which includes all remuneration elements that are not fixed.	
Para. 9 Definitions	A respondent recommends that the definition of gender neutral remuneration policies include the priority and commitment to actively tackle the gender pay gap in investment firms, as well as the commitment that firms address the gender pension gap in their remuneration policies. With regard to the definition of 'gender pay gap', a respondent notes that it does not take into account the type of work, nor does it include the level of responsibility or the experience, and therefore a gender pay gap, where calculated in this manner, does not meet the purpose of gender neutral remuneration policies. Additionally, it is suggested replacing the term 'earnings' with 'remuneration' and to switch from 'hourly' (which is not a common practice in the financial/banking industry) to 'full-time annual remuneration awarded' in order to be consistent with paragraph 25.	In line with work published by the European Parliament, the gender pay gap is the difference in average gross hourly earnings between women and men. It is based on salaries paid directly to employees before income tax and social security contributions are deducted. Calculated this way, the gender pay gap does not take into account all the different factors that may play a role, for example education, hours worked, type of job, career breaks or part-time work. The gender pay gap indicates more than just the difference in hourly or annual gross remuneration for the same job (which should not be different at all), but provides information on how successfully equal opportunities have been provided within society and within the investment firm. The GL were amended to replace unclear terms.	GL amended
Question 2. Is the section on gender neutral remuneration policies sufficiently clear?			
Equal value of work	Some respondents suggest further strengthening the language on equal value of work, drawing inspiration from (or referring to) documents such as the Commission Recommendation C(2014) 1405 final, para. 10, or the Commission Staff Working Document SWD/2013/0512, or from the rulings of the ECJ. It is observed that, especially when it comes to topics such as severance payments and evaluation of value of work based on the contract type in question, great care should be shown to ensure the promotion of equality and impartiality.	The criteria included in the Commission Recommendation have been included; however, the recommendation does not provide for an exhaustive enumeration of criteria.	GL amended

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
Gender neutral policies and ESG factors	A respondent recommends clarifying that gender neutral remuneration policies also be aligned with investment firms' sustainability performance objectives on social issues (the 'S' of ESG) and explaining how such policies are linked with internal gender equality performance targets. This would ensure firms account for the way their governance operations impact on gender equality, and action plans are set out when remuneration policies do not meet performance targets on reducing the gender pay and pension gap.	Remuneration policies must be aligned with their risks; ESG risk factors are relevant to the risk profile of investment firms. Moreover, investment firms are obliged in line with the national implementation of Directive 2006/54/EU to ensure equal opportunities. The provisions on equal opportunities and anti-discrimination have been reviewed.	GL amended
Para. 23 Gender neutral remuneration policies	A respondent suggests deleting the reference to '*all related employment conditions that have an impact on the pay per unit of measurement or time rate should be gender neutral*', since it goes beyond gender neutral remuneration policies. The same respondent claims that the guidelines significantly broaden the scope of gender neutral remuneration policies as required by the IFD by including issues related to gender equality policies (e.g. career development, succession plans), and consequently requests the deletion of the second sentence of paragraph 23.	Other conditions have an impact on the value of pay received. Some other benefits may have a material value in financial terms. See also comment above.	No change
Para. 25 Gender neutral remuneration policies	A respondent suggests using '*working time arrangements*' as unit of measurement, as it is simpler and clearer than 'the remuneration awarded'.	The section has been revised to provide further clarity.	GL amended
Para. 26 Documentation on gender neutral remuneration policies	Many respondents do not support the wording of paragraph 26, since the documentation requirements are excessively prescriptive, onerous and time-consuming, do not focus on categories of job positions and do not reflect cross-border firms' obligations to comply with Member State rules and guidance in respect of equal pay. It is observed that job descriptions for all staff members are not the norm and that the aim of	The mandate of the EBA is to ensure compliance with the principle of equal pay for male and female workers for equal work or work of equal value, thus there is a need to identify the jobs considered as equal or of equal value.	GL amended

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
	equal pay for male and female workers for equal work or work of equal value could be achieved through a general documentation and determination of the positions (and not of each staff member) based on assessments and scoring systems on skills, knowledge, activities or tasks. In the same vein, it is requested to specify that investment firms retain flexibility in determining how to properly document that a gender neutral remuneration policy is being applied.	The GL have been amended to allow the use of job classification systems. The provisions of the guidelines have been clarified.	
Para. 27 Determination of the value of work	A respondent asks for the paragraph be rephrased to take into account additional aspects to determine the remuneration level, beyond the equal value of work. In particular, it is pointed out that the nature of the employment contract, including if it is temporary or a contract with an indefinite period (letter e), does not provide any information as to the value of work. A respondent recommends adding an item on 'specific skills or competence of staff' and changing the wording of point h): '*h) appropriate benefits, including the payment of additional **voluntary** household and other allowances to staff with dependent **family members (e.g.** children**, other closed relatives)***.'	The guidelines have been better aligned with Commission Recommendation C(2014) 1405 and further clarifications have been made.	GL amended
Para. 38 Gender neutral remuneration policies and HR	A respondent suggests adding to the paragraph that: '***The HR function should also ensure that the remuneration policy is consistent with obligations on gender neutrality and equal treatment of different genders***'.	The remuneration policy must be gender neutral. This fact is true for all aspects of the remuneration policy and its development, implementation or review, without this being mentioned in each and every part of the guidelines.	No change
Para. 59 Gender pay gap	A respondent is concerned that publishing gender pay gap reports for management bodies is highly confidential and conflicts with GDPR requirements, given the very small size of the sample. It is therefore requested that this requirement be clarified as being for internal documentation only.	The guidelines do not require the publication of data that would lead to a breach of GDPR requirements. The supervisory review of the gender pay gap and its monitoring is a lawful purpose mandated under the IFD. In addition	No change

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
		investment firms are required to disclose certain remuneration data for their management body.	
Question 3. Are the sections on the remuneration committee sufficiently clear?			
Remuneration committee and proportionality	Some respondents observe that the draft EBA guidelines apply the exact same requirements as currently applied to the largest, riskiest banks, to a broad range of small investment firms, which pose far less risk to the financial system, and urge the EBA to reconsider such approach.	Certain investment firms are required under the IFD to have a remuneration committee. The guidelines provide already for some proportionality for firms with smaller boards.	No change
Remuneration committee and engagement with shareholders	A respondent asks for the guidelines to clarify that the remuneration committee should actively engage with shareholders on gender equality issues within firms' direct operations and across their supply chains, and should also explain in its reports what engagement with investors has taken place and how the outcomes of these engagements have been integrated into the subsequent remuneration policies.	While engagements with shareholders might be required under the shareholder rights directive, the IFD does not contain such a requirement.	No change
Para. 50 Composition of the remuneration committee	Some respondents raise doubts about the requirement for a gender balanced remuneration committee, since setting up such a committee could be problematic and burdensome, and investment firms may at times be constrained in the selection of committee members, so that strict gender balance may not be practical at all times. The EBA is therefore advised to clarify that the expectation is for investment firms to use their best efforts to have a gender balanced remuneration committee over time. Some respondents note that the wording used in paragraph 50 is relatively unclear as to the definition of balanced, and in particular how this might apply to remuneration committees with an odd number of committee members, and proposes updating it to specify that '*the remuneration committee should be **appropriately** gender balanced*'.	The requirement Is included in the IFD and cannot be altered by guidelines. The term balance does not imply that there should always be a 50% representation of the male and female gender. With regard to the population of identified staff, it is assumed that the results of collective arrangements are less relevant.	No change

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
	Another respondent welcomes the specific reference made to the inclusion of employee representatives in the remuneration committee, but would like it to be highlighted that where national and sectoral collective agreements have been reached, these should form the base for the work of the remuneration committee.		
Para. 51 Independence of members of the remuneration committee	A few respondents note that the requirement for remuneration committee members to be independent appears to be replicated from the existing guidelines under CRD and is not supported by the Level 1 text, which only requires members of the remuneration committee to comprise 'members of the management body who do not perform any executive function in the investment firm concerned'.	Having independent members within the management body and remuneration committee is part of the provisions of robust governance arrangements which are required under IFD.	No change
Para. 51 Independence of members of the remuneration committee	Some respondents ask for a clarification that, as the paragraph is meant to address conflicts of interest, other alternative measures can be taken, as long as these are efficiently addressing these risks.	The guidelines have been clarified. In any case there should be measures to ensure that decisions are not unduly influenced by conflicts of interests.	GL amended
Para. 58 Meetings of the remuneration committee	Some respondents deem it unnecessary for members of the risk committee to participate in all meetings of the remuneration committee. It should be clarified that they should have the possibility to participate when appropriate. Moreover, there would be no point in requiring a member of the remuneration committee to participate in each meeting of the risk committee. All matters regarding the tasks of the remuneration committee should be discussed within the remuneration committee where a member of the risk management committee can provide input.	The comment has been accommodated.	GL amended
Question 4. Are the guidelines on the application of the requirements in a group context sufficiently clear?			

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
Scope of the group application	A respondent asks for the scope of the group application on a consolidated level to be clarified exhaustedly in only one section (such as section 3).	References to the IFD/IFR requirements on prudential consolidation have been added. There is additional work conducted at EBA to clarify the issue of consolidation further.	GL amended
Terms used	Some respondents request that all references to 'subsidiaries', 'investment firms as subsidiaries', 'consolidating parent investment firm', 'consolidating institution', 'EU parent investment firm' be reviewed, alleging that the terms used would not comply with the definitions and scope of the prudential consolidation of IFD/IFR framework in all cases (e.g. the parent company of an investment firm group may not be an investment firm).	The guidelines contain a definition of consolidating institution that includes both the consolidating institution being an institution or an investment firm.	No change
Investment firms belonging to banking groups	A respondent deems it helpful to clarify how the guidelines apply to investment firms as subsidiaries of a banking (or insurance) group, since under the new Article 109(4)a) CRD V, these investment firms in Member states are required to apply the remuneration rules on an individual basis, independent of the fact that they are subsidiaries of a banking group.	The scope of application of the guidelines is clearly set out. It includes investment firms that are part of a banking group.	No change
Para. 69 Subsidiaries within investment firms' groups	Several respondents, while acknowledging that IFD does not have a provision equivalent to Art. 109 CRD, think that the EBA should (and is entitled to) provide guidance on how the remuneration rules in the IFD should apply within groups of investment firms. They recommend that the EBA clarify in the guidelines that if a subsidiary of an investment firm is subject to another EU remuneration regime (or would be if it were established in the EU), then that subsidiary will only have to apply its sectoral requirements, without being required to apply the requirements of the IFD (other than any requirements explicitly specified by the EBA). The only exception to that would be for any individuals working for the subsidiary who are mandated to perform	Article 25 IFD determines that where Section 2 (including remuneration requirements) applies and prudential consolidation as referred to in Article 7 of Regulation (EU) 2019/2033 is applied, Member States shall ensure that this Section is applied to investment firms on an individual and consolidated basis. This means that the consolidating investment firm must ensure that the provisions are applied consistently in the scope of consolidation as if all consolidated entities would form one investment firm.	GL amended

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
	professional activities that have a direct material impact on the risk profile or business of the IFD firms within the consolidation group. A respondent notes that in case of parts of the remuneration policy falling within the scope of co-determination or collective bargaining rights, the consolidating institution may not be able to enforce the remuneration policy without undergoing the necessary procedures with the employee side, and recommends adding to the end of the last sentence of paragraph 69: '***with no prejudice to the rights of employee representatives and trade unions under national law***'.	The IFD does not provide for any exclusion of firms from the consolidated application, i.e. it includes also small and not interconnected investment firms that are not subject on an individual basis to the remuneration provisions and also firms that are subject to a specific remuneration framework themselves. The GL have been clarified.	
Para. 70 Group's remuneration policy	A respondent welcomes the clarification that specific remuneration requirements of subsidiaries should be taken into account at consolidated level, but requests amendments in view of some general remarks on the application of the remuneration policies to all staff and on the scope of prudential consolidation as referred to in Article 7(1) IFR. Another respondent asks for clarification on the 'specific remuneration requirements of subsidiaries', since such requirements always have to be taken into account and are independent of gender neutrality provisions.	See comments above	No change
Para. 72 Staff with a material impact on the group's risk profile	A respondent requests deleting the reference to identified staff that has a material impact on the group's risk profile, since such category of staff is not required by Article 30(1) IFD. Moreover, as long as the IFD framework does not require a bonus cap for investment firms and the EBA argues that the IFD remuneration requirements are consistent with other sector-specific requirements, there would be no need to establish a category of staff that has a material impact on the group's risk profile.	The provisions apply on a consolidated basis and require specific provisions to be applied to identified staff (risk takers). Hence, their identification is required on an individual and consolidated basis.	No change

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
Para. 73 Staff secondment	Some respondents deem it disproportionate to expect an overseas entity not subject to the remuneration provisions of Directive (EU) 2019/2034 to set up and administer a 'European remuneration program' only for a limited number of individual employees who may periodically be carrying out short, ad-hoc projects. They therefore believe that the application of European remuneration rules to seconded staff should include a *de minimis* threshold, which could consist of a stay of at least three or six months.	The guidelines need to be read together with the RTS on identified staff. Staff on short-term secondments would not become identified staff. The minimum period established in the RTS is three months.	No change
Para. 75 Third country groups	A respondent alleges that the application to investment firms in Member States on an individual level is not addressed with proper terms in the group context, and requests that exemptions for subsidiaries established in third countries, as addressed in Article 25(4) IFD, should also be clarified in in the guidelines. Moreover, in view of a better understanding, it could be helpful to separate the third-country approach from the application to investment firms on an individual basis.	Subsidiaries of an EU parent in a third country are within the scope of consolidated application of the IFD requirements unless the application of the remuneration requirements in this country is unlawful.	No change
Question 5. Are the guidelines regarding the application of waivers within section 4 sufficiently clear?			
Individual vs. consolidated level	Some respondents ask the EBA to clarify that waivers can be obtained if the assets of the particular entity are below the relevant threshold (i.e. EUR 100 million or the increased/lowered threshold) and that it is not necessary for the assets of the consolidation group to be below EUR 100 million (i.e. an investment firm should be able to avail itself of the waiver where, on an individual basis, it does not exceed the relevant threshold).	The scope of application of provisions and waivers is set within the IFD. Firms can apply waivers on the individual level, where implemented by Member States, with the thresholds applicable under national law. The same applies at the consolidated level with regard to the Member State where the consolidating firm is located regarding the staff that has been identified on a consolidated level, even if employed in a subsidiary.	GL amended

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
Para. 85-86 Application of waivers	Some respondents ask to review and amend the terms used in the group context, since the parent company of an investment firm group may not be an investment firm and the determination of the effective ratio between the variable and fixed remuneration should be limited to identified staff. A respondent does not understand why severance payments under para. 162 of the draft guidelines are not considered when calculating the general ratio of variable and fixed remuneration, but are instead counted for the calculation of the ratio for the purpose of the waiver under Art. 32(4)(b) IFD. It is therefore recommended adding to letter d: '***Severance payments covered by para. 162 are not taken into account***'. A respondent sees no point in establishing a specific exchange rate in the guidelines and recommends deleting the reference to it, or stressing that the rate to be used should be part of the entities remuneration policy before each yearly exercise is launched.	The requirements in Articles 30 and 32 IFD, including the requirement to set a maximum ratio in the policy, apply to identify staff on an individual and consolidated level. Severance payments are variable remuneration and are taken into account when calculating the thresholds. See also the additional explanations in the summary of the EBA response.	No change
Para. 85	A respondent also invites the EBA to amend paragraph 85 so as to explicitly state that, where the relevant applicable threshold is exceeded on an individual basis, it is not possible for the investment firm to avail itself of a waiver on the grounds that on a consolidated basis, the (higher) applicable threshold in another Member State is not exceeded.	While this is correct, it is clear without providing additional guidelines as all requirements apply also on an individual level.	No change
Para. 244 Waivers and deferral	A respondent requests an amendment to the paragraph to clarify that '*without prejudice to the application of waivers under Article 32(4)*' should be interpreted as meaning '*subject to the application of waivers under Article 32(4)*'.	The formulation is a standard formulation for legal texts. The application depends on the national implementation by Member States.	No change
Question 6. Is section 9 on severance payments sufficiently clear?			

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
Severance payment framework	Some respondents suggest that the full detail of an investment firm's severance payment framework should remain confidential to the firm and for review by local regulators and supervisory bodies as appropriate, rather than being replicated in full detail within the remuneration policy itself, which could instead refer to the main principles and confirm existence of a more detailed framework. According to the respondent, the publication of the detailed severance payment framework could create disproportionate legal risks for firms and increase complexity in employee relations.	Severance payments are sometimes based on standard formulas, e.g. that reflect past court cases, or can be negotiated individually. It is therefore not necessary to develop a framework for severance payments that covers each and every possible situation. However, the remuneration policy should provide for a framework; whenever there would be a deviation from the framework, a decision of the management body would be necessary.	No change
Notice pay	Some respondents welcome the confirmation that notice pay is excluded from severance payments, but suggest clarifying that any other standard payments related to notice periods are also excluded.	The guidelines have been clarified.	GL amended
Para. 156 Severance payments and normal variable remuneration	A respondent observes that: (i) not 'any' additional payments in the context of the termination of the mandate of a board member should be considered as 'normal variable remuneration'; (ii) the reference to 'member of the management body' should be deleted, since non-executive members of the management body have a remuneration structure that is different to more 'traditional' risk takers; (iii) the reference to 'regular end' of 'a contractual period' should be dropped, as it would result in a new unregulated concept, different from 'early' termination and might prove an issue in jurisdictions where indefinite contracts are widely used.	The guidelines and the concept of early termination have been clarified with regard to different types of contracts. Also indefinite contracts have a regular end. The reference to members of the management body has been retained, the treatment of non-executive directors may differ between Member States. In some cases they receive also remuneration and not only participation fees.	GL amended
Para. 157 Labour dispute	A respondent recommends amending point e), as a court ruling would be necessary for each case, which is not workable. '*e. The investment firm and a staff member agree on a settlement in case of* ***a potential or*** *an actual labour dispute that could potentially*	The GL do not have the intention to force each and every severance payment to be brought in front of the court. The GL have been clarified.	GL amended

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
	bring an action in front of a court *~~lead to a court ruling~~, to avoid a decision on a settlement by the courts*'.		
Para. 162 Exemptions	A respondent asks the EBA to clarify why non-competition clauses have been included separately from other severance payments and to amend the paragraph, as it considers transactional severance payments as variable remuneration (to be included in the variable/fixed ratio and to be deferred).	The provision allows for the grant of gardening leave periods after the contract has ended. The GL have been further clarified regarding payments that are made for the fact that staff cannot take up an occupational activity at a competitor.	No change
Question 7. Are the provisions on performance criteria sufficiently clear, which other performance indicators, such as regarding the performance of business units or portfolios, are used to determine the variable remuneration of identified staff?			
Para. 178 and 249 Remuneration of members of the management body in its supervisory function	Some respondents observe that in smaller to medium-sized investment firms with unitary board structures, the management body fulfils multiple functions (a supervisory function as well as an executive management function) and is accountable for the day-to-day management of the undertaking, so that its role cannot be separated from its role as a collective supervisory function. Another respondent does not agree that members of the supervisory function may receive variable remuneration only in exceptional cases, which sets the bar too high. While acknowledging the importance that remuneration of members of the supervisory function should not create conflicts of interest, it is observed that: (i) conflicts can be managed, for example, through the setting of an appropriate maximum ratio between fixed and variable remuneration; (ii) it is disproportionate for smaller firms, which do not necessarily have separate management and supervisory functions, to be subject to such standard.	The functions of the board are defined in the IFD and MiFID and depend also on national company law. The approach is consistent with Article 4(1)(36) of Directive 2014/65/EU: '…the managerial and supervisory functions of the management body are assigned to different bodies or different members within one body …'. The EBA is aware that there are exceptions to this principle in small investment firms. Members in the management body that have a management function can receive variable remuneration. It should be noted that the guidelines apply only to firms that are subject to specific remuneration provisions under IFD. The guidelines have been clarified.	GL amended
Para. 196	A respondent requests the term 'asset management' be replaced with the term 'portfolio management'. Asset management is a term used by	The GL apply to firms that are subject to the specific remuneration provisions under IFD.	GL amended

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Variable/fixed ratio	the European Directives (AIFMD and UCITS Directive) dealing with collective investment undertakings. Portfolio management as a MiFID service should be used under the IFD framework.	The wording has been revised to cover all activities that involve the management of assets within the investment firm.	
Para. 217 Performance criteria	Some respondents appreciate that quantitative criteria should cover a period which is long enough to properly capture the risk taken by identified staff members, business units and the investment firm, but ask for greater clarity on whether one year is acceptable for certain non-investment-related roles, where multi-year performance is less appropriate and the risks relevant to the role (e.g. reputational and operational risk) can be assessed on an annual basis.	The system of performance indicators depends on the business cycle of the firm. In many cases, the main performance criteria for the annual bonus of most staff are aligned with the financial year. In particular, for the management body, a multi-year framework might often be more appropriate because it is responsible for setting the firm's strategy.	No change
Question 8. Is the section on the pay-out in instruments sufficiently clear?			
Para. 243 Balance between instruments and cash	Some respondents point out that the paragraph should better reflect the fact that the requirement is to have a balance between non-cash instruments and cash (as opposed to having a balance between equity, equity-linked instruments, other instruments and cash).	The use of different types of instruments, in particular if a higher amount of variable remuneration is awarded, can contribute to a better risk alignment. However, there is no hard requirement to use a balance of instruments. The guidelines have been corrected and clarified.	GL amended
Para. 249 Deferral's length	A respondent notes that the minimum requirement of a three-year deferral period leaves no room to apply the principle of proportionality and goes beyond what is required in the Level 1 text (no minimum deferral period is set for the management body in the Level 1 text). Some respondents also note that the last sentence of the paragraph is not drafted with due regard to the proportionality principle and should be removed.	The IFD sets a minimum requirement for the application of the deferral requirement. The proportionate application is starting at this length of the deferral period, in cases where deferral has to be applied. Most medium-sized investment firms will be able to benefit from the waivers of the requirement to defer variable remuneration. Para. 249 has been amended and the last sentence has been removed.	GL amended

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Para. 250 Variable remuneration of a particularly high amount	With regard to variable remuneration of a particularly high amount, a respondent is concerned that thresholds set by competent authorities and/or through remuneration benchmarking reports covering all investment firms will span a broad range of the financial services industry and will not sufficiently distinguish between investment firm types, resulting in a disproportionate outcome. If investment firms are required to consider benchmarking reports, it is important that such benchmarking exercises are sufficiently granular to distinguish between types of investment firms, for example by breaking them down according to what MiFID II services and activities the investment firm performs.	Payment levels differ between Member States. As the requirement is applied to variable remuneration, it is appropriate to consider separately the variable and fixed remuneration components. The GL have been amended as this could be based on the absolute amounts. The EBA will develop a remuneration benchmarking exercise for investment firms; however, benchmarks should be considered, but do not provide hard thresholds.	GL amended
Para. 261 Use of alternative arrangements	Regarding the use of alternative arrangements by investment firms not issuing eligible financial instruments, many respondents wonder whether subparagraph (a) of paragraph 261 reads as a declaratory statement or as a query. If subparagraph (a) were to be understood as a declaratory statement, this would deviate from the Level 1 text, since many investment firms are unlisted stock corporations and do not issue shares, other than to the founders of the firm (which could be individuals, or a corporation when the investment firm is held by a holding company). If these firms were required to issue new shares to a high number of individuals, this would substantially increase the regulatory burden and costs for those firms and might also materially affect their ownership structures (e.g. in the case of wholly owned subsidiaries within alternative asset management groups). Finally, it is suggested that for unlisted MiFID firms within alternative asset management groups, carried interests could be the sort of 'alternative arrangements' that competent authorities should be encouraged to approve.	Firms that issue shares have instruments available and therefore competent authorities cannot approve alternative arrangements. Where shares are issued, in any case share-linked instruments can be used without any dilution of shareholdings. Investment firms can also use other types of instruments for the pay-out of variable remuneration as specified in the IFD and the delegated regulation mandated under IFD. Under Article 32(1)(k) of the IFD, alternative arrangements can only be approved where an investment firm does not issue any of the instruments referred to in point (j) and if they fulfil the same objective. Further conditions for alternative arrangements are specified in a Commission Delegated Regulation that is based on the draft submitted by the EBA.	GL amended

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
		The wording has been clarified.	
Para. 269 Payment in instruments	Some respondents propose the following amendment: '*The ratio of variable remuneration that is paid out in instruments should be calculated as the quotient between the amount of variable remuneration awarded in instruments and the sum of the variable remuneration awarded in cash, instruments and in* ***any*** *other* ***form*** ~~***benefits***~~.'	The comment has been accommodated.	GL amended
Para. 274 Retention period for financial instruments	Some respondents do not support the minimum twelve-month retention period for financial instruments, since it contradicts the flexibility granted to investment firms by paragraphs 270-272 to determine the retention period that is appropriate to their risk profile and long-term interests, and in some scenarios a lower retention period (such as six months) may be more appropriate. It is pointed out that the ESMA Guidelines on Sound Remuneration Policies under UCITS and AIFMD do not mandate a minimum twelve-month retention period, and that some national competent authorities recommended a minimum six-month retention period under UCITS and AIFMD. The respondents request paragraph 274 be removed, so as to have a better alignment to UCITS and AIFMD rules, or alternatively a minimum six-month retention period be mandated, as opposed to a twelve-month period.	A sufficiently long retention period ensures a better alignment with the risk of the investment firm and facilitates the application of clawback. A shorter retention period would not meet this objective and such a remuneration policy would therefore not promote sound and effective risk management as required under Article 26 (1)(d) IFD. In particular, where no deferral is applied, even longer periods are in many cases appropriate.	No change

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